



FINANCIAL AUDIT DIVISION REPORT

Minnesota Veterans Home in Minneapolis

Special Review

January 1, 2010, through June 30, 2011

December 1, 2011

Report 11-28

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OFFICE OF THE LEGISLATIVE AUDITOR

State of Minnesota • James Nobles, Legislative Auditor

December 1, 2011

Representative Michael Beard, Chair
Legislative Audit Commission

Members of the Legislative Audit Commission

Larry Shellito, Commissioner
Minnesota Department of Veterans Affairs

Shelley Kendrick, Administrator
Minnesota Veterans Home-Minneapolis

This report presents the results of our special review of the cashiering function and resident account financial activity at the Minnesota Veterans Home in Minneapolis' business office for the period January 1, 2010, through June 30, 2011.

As required by *Minnesota Statutes* 2011, 3.975, we are referring this special review to the Attorney General and the Hennepin County Attorney. The Attorney General has the responsibility to recover state funds that were used inappropriately, and the county attorney will be asked to determine whether criminal proceedings are warranted.

This special review was conducted by Michael Hassing, CPA, CISA (Audit Manager) and Sonya Johnson, CPA, CFE (Director of Investigations).

This report is intended for the information and use of the Legislative Audit Commission and the management of the Minnesota Veterans Home in Minneapolis. This restriction is not intended to limit the full distribution of this report, which was released as a public document on December 1, 2011.

We received the full cooperation of the home's staff while performing this special review.

A handwritten signature in black ink, reading 'James R. Nobles'.

James R. Nobles
Legislative Auditor

A handwritten signature in black ink, reading 'Cecile M. Ferkul'.

Cecile M. Ferkul, CPA, CISA
Deputy Legislative Auditor

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Report Summary

Conclusion

The resident accounting records at the Minnesota Veterans Home in Minneapolis showed evidence of possible financial wrongdoing. For the period from January 2010 through June 2011, approximately \$6,800 of documented receipts from 20 residents did not trace to bank deposits or resident accounting records. In addition, the home's resident accounting records showed delays in recording approximately \$16,500 of resident receipts, which could be an indication of fraud.

The Minnesota Veterans Home in Minneapolis did not have adequate internal controls to ensure that it safeguarded resident funds and accurately recorded resident account financial activity in its accounting records.

Key Findings

- The Minnesota Veterans Home in Minneapolis did not deposit and record in its residents' accounts approximately \$6,800 received from residents by the business office. In addition, there were delays in depositing and recording \$16,500 of other receipts, possibly indicating fraud. ([Finding 1, page 5](#))
- The Minnesota Veterans Home in Minneapolis did not establish effective controls to mitigate the increased risk that error or fraud could occur without detection because of the cashier's incompatible duties. ([Finding 2, page 6](#))

Audit Objective and Scope

Our special review of the cashiering function and resident receipt activity at the Minnesota Veterans Home in Minneapolis covered the period from January 2010 through June 2011 and included internal controls over receipts for residents' accounts. During the period from January 2010 through June 2011, the home recorded approximately \$10.5 million as received on behalf of its residents. This was not a complete review of all financial activities at the Minnesota Veterans Home in Minneapolis.

Background

In early July 2011, management of the Minnesota Veterans Home in Minneapolis notified the Office of the Legislative Auditor that family members of two residents had identified certain financial transactions that they thought were in error. In following up on those transactions, the home became concerned that the transactions may indicate wrongdoing by someone in its business office. The home asked the Office of the Legislative Auditor to further investigate the home's records supporting its residents' financial activity. Based on our preliminary assessment of the concerns, we decided to conduct a special review to determine if there was evidence of possible financial wrongdoing and, if so, to identify deficiencies in the home's internal controls that may have allowed the wrongdoing to continue without detection.

The Minnesota Veterans Home in Minneapolis is one of five veterans homes operated by the Minnesota Department of Veterans Affairs. Shelley Kendrick is the home's current administrator. Over the past several years, the business office had significant turnover in its key managerial and administrative staff. The cashier, who reports to the business office manager, is responsible for the collection and initial recording of the home's receipts, including receipts to pay for residents' cost of care, donations, and residents' trust account monies. During the period from January 2010 through June 2011, the home recorded approximately \$10.5 million as received on behalf of its residents.

Our past audits of the Minnesota Veterans Home in Minneapolis have reported significant weaknesses in the home's internal controls.¹ Our most recent report, issued in October 2010, included a finding about the lack of separation of incompatible duties in certain business office functions, including the cashiering and recordkeeping functions. Separation of incompatible duties prevents one employee from having control over two or more parts of a transaction. For example, an employee who has the responsibility to ensure that receipts are adequately safeguarded and deposited in the bank should not also be responsible for posting those receipts to the accounting records or reconciling between the receipts deposited and recorded. When the duties of safeguarding, recording, authorizing, and reconciling financial transactions are not segregated, the risk of error or fraud occurring without detection increases.

¹ Office of the Legislative Auditor's Financial Audit Division Reports [05-43](#), July 22, 2005; [08-32](#), November 26, 2008; and [10-33](#), October 14, 2010.

Objective, Scope, and Methodology

We examined the Minnesota Veterans Home in Minneapolis' cashiering function and resident account financial activity from January 1, 2010, through June 30, 2011. Our objective was to answer the follow questions:

- Did the Minnesota Veterans Home in Minneapolis' resident accounting records show evidence of possible financial wrongdoing?
- Did the Minnesota Veterans Home in Minneapolis have adequate internal controls over its residents' accounts to ensure that it safeguarded resident money and accurately recorded resident account financial activity in its accounting records?

To answer these questions, we interviewed various personnel of the Minnesota Veterans Home in Minneapolis to understand the home's policies, procedures, and practices, and we identified internal controls. We examined all records supporting resident account transactions between January 1, 2010, and June 30, 2011, including records supporting receipts and deposits of resident funds, authorizations for withdrawals of resident funds, and the residents' individual account statements prepared by the home.

Conclusion

The resident accounting records at the Minnesota Veterans Home in Minneapolis showed evidence of possible financial wrongdoing. For the period from January 2010 through June 2011, approximately \$6,800 of documented receipts from 20 residents did not trace to bank deposits or resident accounting records. In addition, the home's resident accounting records showed delays in recording approximately \$16,500 of resident receipts, which could be an indication of fraud.

The Minnesota Veterans Home in Minneapolis did not have adequate internal controls to ensure that it safeguarded resident funds and accurately recorded resident account financial activity in its accounting records.

The following *Findings and Recommendations* section explains the results of our special review.

Findings and Recommendations

The Minnesota Veterans Home in Minneapolis did not deposit and record in its residents' accounts approximately \$6,800 received from residents by the business office. In addition, there were delays in depositing and recording \$16,500 of other receipts, possibly indicating fraud.

Finding 1

Our review of receipt transactions from January 2010 through June 2011 confirmed the suspicion of some residents' families that the home did not accurately account for cash receipt transactions or appropriately record resident account financial activity. We identified the following discrepancies:

- The home had prenumbered receipts for about \$6,800 from 20 residents that did not appear on the daily transaction logs and were not included in the home's bank deposits.² In addition, because the transactions were not on the daily transaction logs, the home never recorded the transaction in the residents' accounts.³ For example, on April 6, 2011, the cashier prepared a prenumbered receipt for \$1,396.69 but the daily transaction log and bank deposit he also prepared only included a \$16.69 check for that resident. The resident's representative noticed the \$1,380 discrepancy when reviewing the resident's monthly account statement. When the representative contacted the home, she stated that in addition to the check, she had given the home \$1,380 in cash as evidenced by her copy of the prenumbered receipt.
- On some days, the cashier prepared prenumbered receipts (ranging from \$25 to \$3,600, and totaling approximately \$16,500) for money received from residents that did not appear on that day's transaction log and was not included in that day's bank deposit. Because the receipts were not recorded on the daily transaction log, the home did not record them in the residents' accounts. However, at a later date (anywhere from few days to six weeks later), the cashier recorded cash on the daily transaction log and included cash in the bank deposit that agreed with the amount previously received. This subsequent transaction did not have a corresponding prenumbered receipt.

For example, on April 1, 2010, the cashier wrote a prenumbered receipt for \$3,605.50 received on behalf of a resident. On that day, the daily

² The home's daily transaction log should include all resident financial activity, including receipts and withdrawals. The home used the daily log to prepare the bank deposit and to post financial activity to the residents' accounts.

³ Since our audit, the home has restored \$1,430 to two residents' accounts out of its operating budget based on evidence sufficient to show that the home had received but not recorded the money.

transaction log only included checks totaling \$1,905.50 for that resident, resulting in a \$1,700 discrepancy. Subsequently, on May 4, 2010, the daily transaction log and the bank deposit included a cash receipt of \$1,700 for this resident. There was no prenumbered receipt to support this transaction. A common type of fraud is to use later receipts to cover for previous theft of funds to avoid detection.

When we asked the cashier about the inconsistencies and timing differences between the prenumbered receipts, the daily transaction logs, and the bank deposits, he acknowledged that he had prepared the documents, but he was unable to provide any explanation for the discrepancies. Also, because the cashier told us that he did not always prepare a prenumbered receipt, residents may have deposited other money with the business office that was not deposited in the home's bank account or recorded in the residents' accounts.

During a period between the middle of April 2011 and early July 2011, when the regular cashier was on an extended leave and another employee performed his duties, we did not find any discrepancies between the prenumbered receipts, the daily transaction logs, the bank deposits, and the transactions recorded in the residents' accounts.

Recommendation

- *The home should identify and resolve all discrepancies in the residents' accounts.*

Finding 2

The Minnesota Veterans Home in Minneapolis did not establish effective controls to mitigate the increased risk that error or fraud could occur without detection because of the cashier's incompatible duties.

The Minnesota Veterans Home in Minneapolis lacked fundamental internal controls in its receipt processes to ensure that it accurately accounted for resident receipts. Because the cashier had incompatible duties (he had direct access to cash and checks submitted by residents for deposit with the home, prepared the daily transaction log of resident financial activity,⁴ and prepared the bank deposits), the home designed controls to mitigate the increased risk of error or fraud not being detected. However, those controls had the following deficiencies:

- The cashier did not always provide a receipt for money submitted to the business office. He told us he only provided a prenumbered receipt at the request of a resident or their representative. Because the weakest point in a receipt process is before a receipt is recorded, the home's policies required that the resident or his representative always be given a written receipt that

⁴ The home used the daily transaction log to verify the accuracy of the amount deposited in the bank and to record financial activity in the resident's accounts.

showed the resident's name and account number, the amount deposited, and the signature of the business office employee receiving the deposit.⁵ In addition, the home's policies required, "as an added precaution," that the home perform random audits of the prenumbered receipt books.⁶ We saw no evidence that the home had performed any random audits of the prenumbered receipt books, and the home was unaware that the cashier was not always providing residents with a receipt, as required by policy.

- The home's reconciliation process did not ensure that receipts recorded in the prenumbered receipt book agreed with the receipts recorded on the daily transaction log and were included in the bank deposit. The home's reconciliations showed that the daily transaction log always agreed to the bank deposit amount; however, it did not identify that the cashier had omitted some prenumbered receipts from the daily transaction log.

Because of these internal control weaknesses, the home had an unacceptable risk that error or fraud could occur without detection. As a result, the home was dependent on residents or their representatives to monitor the accuracy of financial activity recorded on the residents' account statements.⁷ Residents or their representatives were limited in their ability to quickly identify a missing transaction or a timing discrepancy because the residents' account statements were only available monthly or quarterly, depending on the type of account.⁸ Regardless, it is not acceptable for the home to rely on reviews performed by residents or their representatives as a primary control to ensure that the home adequately safeguarded and accurately accounted for the resident's money.

State statutes allow the home to accept money from residents for safekeeping purposes and require the home to deposit the money in the state treasury.⁹ State policy requires the home to have internal controls to safeguard assets against loss or unauthorized use.¹⁰

⁵ Minnesota Veterans Home in Minneapolis Policy and Procedure #26-34, *Cashier Operating Procedures*, Procedure 1 (a).

⁶ Minnesota Veterans Home in Minneapolis Policy and Procedure #26-34, *Cashier Operating Procedures*, Procedure 3 (d).

⁷ It was this type of monitoring performed by family members of specific residents that prompted our review.

⁸ Most residents have two types of accounts: a maintenance account and a trust account. A resident's maintenance account shows the billings for care at the home and the resident's payments made for that care. (The home determines a resident's responsibility for their cost of care based on the resident's available assets and income.) Statements for maintenance accounts were available monthly. A resident's trust account shows the resident's personal funds deposited with the home for safekeeping. Statements for trust accounts were available quarterly.

⁹ *Minnesota Statutes* 2011, Chapter 198.265.

¹⁰ Department of Management and Budget Operating Policy and Procedure 0102-01.

Recommendation

- *The Minnesota Veterans Home in Minneapolis should work with the Department of Veterans Affairs to review and revise business office duties, policies and procedures, and internal control practices to ensure the home safeguards and accurately accounts for residents' money.*
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State of Minnesota
Minnesota Veterans Home – Minneapolis
5101 Minnehaha Avenue South
Minneapolis, Minnesota 55417-1699

November 28, 2011

Mr. James R. Nobles, Legislative Auditor
Office of the Legislative Auditor
Room 140 Centennial Building
658 Cedar Street
St. Paul, MN 55155-1603

Dear Mr. Nobles,

Thank you for the investigation completed by your staff. We appreciate that the Office of the Legislative Auditor (OLA) was able to respond immediately when the Minnesota Veterans Home – Minneapolis (MVH-M) contacted the OLA with the initial concern about the possible mishandling of Resident funds. We also appreciate the support and guidance received as the MVH-M continues to evaluate, adjust and improve financial processes.

By design, internal controls provide reasonable, but not absolute, assurance of the achievement of business objectives. The inherent risk of processing cash is particularly high, and skimming cash before its recorded receipt is extremely difficult to prevent. Overall, our internal controls over cash management have improved dramatically over the last three years. However, this follow-up from OLA has helped identify additional changes to address this type of issue, and help prevent it from reoccurrence.

The following are our responses to your Findings and Recommendations:

Finding 1

The Minnesota Veterans Home in Minneapolis did not deposit and record in its residents' accounts approximately \$6,800 received from residents by the business office. In addition, there were delays in depositing and recording \$16,500 of other receipts, possibly indicating fraud.

Recommendation:

- *The home should identify and resolve all discrepancies in the Residents' accounts*

MVH-M Response: **Agree**

During the last week of June 2011, a Resident's spouse contacted MVH-M staff about a \$1,380 discrepancy on a cash maintenance payment she had made. She produced a receipt signed by an MVH-M employee dated April 6, 2011. As a result of this information, MVH-Minneapolis initiated an investigation into the matter and the incident was affirmatively reported to the Legislative Auditor immediately.

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As noted in your report, the Home has already restored \$1,430 to the accounts of two Residents and will restore the approximately \$5,370 to the remaining 18 residents. If more Residents or their representatives come forward with concerns or allegations, the Home will investigate each thoroughly and credit Resident accounts when appropriate.

Responsible Persons: MVH-M Administrator
 MVH-M Business Manager

Estimated Completion Date: No Later Than December 31, 2011

Finding 2

The Minnesota Veterans Home in Minneapolis did not establish effective controls to mitigate the increased risk that error or fraud could occur with detection because of the cashier's incompatible duties.

Recommendation:

- *The Minnesota Veterans Home in Minneapolis should work with the [Minnesota] Department of Veterans Affairs to review and revise business office duties, policies and procedures, and internal control practices to ensure the Home safeguards and accurately accounts for Residents' money.*

MVH-M Response: **Agree**

Starting in July 2011, the Business Office made the following enhancements to its internal controls within the Cashier's Office:

- The office door was re-keyed and vault combination changed. Keys and the vault combination are issued only to employees who have a business need to access the Cashier's Office on a regular basis. The back-up vault combination is controlled by the Business Manager in a tamper evident envelope.
- A computerized Resident trust account ledger system has been implemented. (The previous daily transaction ledger was in Excel spreadsheet format.) All maintenance payments and trust deposits received are entered immediately by the cashier, who generates a receipt in duplicate. A signed copy of the receipt is provided to the payer at the time of deposit.
- Daily receipt reports are generated and balanced to the bank deposit by the cashier and a second employee. All receipts are required to be deposited daily. A third employee matches deposit records to credits to the State Treasury account.
- The computerized ledger system provides for individual login IDs and password controls. The audit log feature allows management to detect any altered or deleted transactions.
- Residents trust account statements are now mailed monthly, along with maintenance account statements. The ledger system also allows us to generate statements for our Residents at the Cashier's Office window upon request.
- Signage outside the window of the Cashier's Office notifies payers and depositors that they are to receive a receipt.
- Operating Policies and Procedures for the Cashier's Office have been updated and are in the process of being implemented.

Responsible Person: MVH-M Business Manager

Estimated Completion Date: No Later Than December 31, 2011

While the health and life safety care of our Residents remains our primary concern, our responsibility goes beyond health and well being. It includes accurately and timely accounting of trust funds, properly managing Home finances and being good stewards of funds. The processes the Home already had in place helped identify and confirm the potential issue as soon as it was brought forward and allowed us to take immediate action.

In conclusion, we believe our internal controls are adequate to reasonably ensure all money received is deposited promptly, recorded in the books, and credited to the correct Resident. We are confident the changes we have made will better serve our Residents and help detect and prevent future incidents.

Sincerely,

A handwritten signature in black ink, appearing to read "Shelley Kendrick" with a stylized flourish at the end.

Shelley Kendrick, Administrator
Minnesota Veterans Home - Minneapolis

CC Larry Shellito, Commissioner, Minnesota Department of Veterans Affairs
Pamela K. Barrows, Deputy Commissioner of Veterans Health Care, Minnesota Department of Veterans Affairs