



OFFICE OF THE LEGISLATIVE AUDITOR
STATE OF MINNESOTA

FINANCIAL AUDIT DIVISION REPORT

Department of Health

Internal Controls and Compliance Audit

**July 1, 2010, through
December 31, 2012**

June 28, 2013

Report 13-13

FINANCIAL AUDIT DIVISION
Centennial Building – Suite 140
658 Cedar Street – Saint Paul, MN 55155
Telephone: 651-296-4708 • Fax: 651-296-4712
E-mail: legislative.auditor@state.mn.us
Web site: <http://www.auditor.leg.state.mn.us>
Through Minnesota Relay: 1-800-627-3529 or 7-1-1



OFFICE OF THE LEGISLATIVE AUDITOR

State of Minnesota • James Nobles, Legislative Auditor

June 28, 2013

Senator Roger Reinert, Chair
Legislative Audit Commission

Members of the Legislative Audit Commission

Dr. Edward Ehlinger, Commissioner
Department of Health

This report presents the results of our audit of internal controls over administration and oversight of grants administered by the Department of Health for the period July 1, 2010, through December 31, 2012. We emphasize that this has not been a comprehensive audit of the Department of Health.

We discussed the results of the audit with the department's staff at an exit conference on June 18, 2013. This audit was conducted by Sonya Johnson, CPA, CFE (Audit Manager) and Susan Kachelmeyer, CPA, CISA (Auditor-in-Charge), assisted by auditors Kayla Borneman, CPA, CFE and Daphne Rhodes.

We received the full cooperation of the department's staff while performing this audit.

Handwritten signature of James R. Nobles in black ink.

James R. Nobles
Legislative Auditor

Handwritten signature of Cecile M. Ferkul in black ink.

Cecile M. Ferkul, CPA, CISA
Deputy Legislative Auditor

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Report Summary

Conclusion

The Department of Health's internal controls over grants were generally adequate to ensure that it accurately reimbursed grant recipients for allowable grant expenditures in accordance with management's authorizations and finance-related legal provisions and accurately recorded these expenditures in the state's accounting systems. For items tested, the Department of Health generally complied with finance-related legal provisions. However, the department had some internal control weaknesses and noncompliance related to grant monitoring procedures.

Findings

- The Department of Health overpaid approximately \$38,000 to several grantees. ([Finding 1, page 5](#))
- The Department of Health did not always comply with state and department grant policies to ensure that it adequately monitored grantees. ([Finding 2, page 6](#))
- The Department of Health paid grantees for costs that were unallowable because the grantee incurred the costs before the start of the grant period. ([Finding 3, page 7](#))
- The Department of Health miscategorized certain grant transactions in the state's accounting system. ([Finding 4, page 8](#))

Audit Objectives and Scope

Objectives

- Internal Controls
- Legal Compliance

Period Audited

July 1, 2010, through December 31, 2012

Programs Audited

- Administration and oversight of grants
-

Department of Health

Agency Overview

The Department of Health's mission is to protect, maintain, and improve the health of all Minnesotans. Its responsibilities include actions to control the spread of infection and illness, promote a healthy environment, help people stay healthy, and safeguard the quality of health care. The department obtains its funding from a variety of sources, including appropriations from the General Fund, Special Revenue Fund, various federal grants, and license and registration fees.

Under its authority, the department provides grants to community health organizations, hospitals, local governments, higher education institutions, and nonprofit organizations.¹ The department competitively awards most of the grants it administers, requiring that the potential grantee submit proposals addressing how the organization will use the money.

In December 2012, we issued a special review on the misuse of grant funds by one of the department's grantees, Sierra Young Family Institute.² The grantee misused almost \$300,000 for costs that we concluded were not related to the purpose of the grant. Because the special review identified that the department's grant oversight processes were not effective in the Sierra Young Family Institute's grant to detect the misuse, we decided to conduct this audit to provide a broader assessment.

For fiscal years 2011, 2012, and 2013 (through December 31, 2012), the state's accounting system recorded the department's grant expenditures as \$142,241,400, \$51,646,764, and \$15,622,565, respectively. However, the accounting records are significantly inaccurate because (as explained in Finding 4) the department miscategorized some grant expenditures as aids.

Objectives, Scope, and Methodology

Our audit of the Department of Health's grant expenditures focused on the following audit objectives for the period July 1, 2010, through December 31, 2012:

- Were the department's internal controls adequate to ensure that it accurately reimbursed grant recipients for allowable grant expenditures in accordance with management's authorizations and finance-related legal

¹ The department operates under *Minnesota Statutes* 2012, Chapter 144, and certain provisions of *Minnesota Statutes* 2012, Chapter 145.

² Office of the Legislative Auditor's Financial Audit Division Report 12-24, *Department of Health, Grant to Sierra Young Family Institute, Inc.*, issued December 6, 2012.

provisions and accurately recorded these expenditures in the state's accounting systems?

- For the items tested, did the Department of Health comply with significant finance-related legal requirements contained in laws, statutes, or state policies?

To meet the audit objectives, we gained an understanding of the Department of Health's financial policies and procedures over grants. We considered the risk of errors in the accounting records and potential noncompliance with relevant legal requirements. We examined samples of financial transactions and reviewed supporting documentation to test whether the agency's controls were effective and if the transactions complied with laws, regulations, policies, and grant and contract provisions.

We conducted the audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives.

We used various criteria to evaluate internal controls and compliance. We used, as our criteria to evaluate agency controls, the guidance contained in the *Internal Control-Integrated Framework*, published by the Committee of Sponsoring Organizations of the Treadway Commission.³ We used state laws, regulations, and contracts, as well as policies and procedures established by the departments of Management and Budget and Administration, as well as the department's internal policies and procedures as evaluation criteria over compliance.

Conclusion

The Department of Health's internal controls over grants were generally adequate to ensure that it accurately reimbursed grant recipients for allowable grant expenditures in accordance with management's authorizations and finance-related legal provisions and accurately recorded these expenditures in the state's accounting systems. For items tested, the Department of Health generally complied with finance-related legal provisions. However, the department had some internal control weaknesses and noncompliance related to its grant monitoring procedures.

The following *Findings and Recommendations* further explain the exceptions noted above.

³ The Treadway Commission and its Committee of Sponsoring Organizations were established in 1985 by the major national associations of accountants. One of their primary tasks was to identify the components of internal control that organizations should have in place to prevent inappropriate financial activity. The resulting *Internal Control-Integrated Framework* is the accepted accounting and auditing standard for internal control design and assessment.

Findings and Recommendations

The Department of Health overpaid approximately \$38,000 to several grantees.

Finding 1

The department made the following overpayments, totaling about \$38,000, to 7 of 40 grantees we tested:

- Department staff overpaid two grantees a total of about \$26,000 because they paid the original invoice and a copy of the invoice.
- Department staff did not detect, as part of the financial reconciliation and invoice review processes, overpayments it had made to five other grantees, totaling about \$12,000. The overpayments ranged from approximately \$300 to \$2,200. Although documentation and invoices provided by grantees either did not reconcile to the reimbursement requests or contained inconsistencies or inaccuracies, department staff did not identify, resolve, or recover grant money for the unsupported costs. Financial reconciliations, required by state policy,⁴ and other reviews allow the department to ensure that documentation supporting costs reconciles to the reimbursement requests that grantees submitted and allow the department to ensure that costs are allowable charges to the grant.

Recommendations

- *The Department of Health should develop a process that prevents or detects duplicate payments.*
- *The Department of Health should ensure that its financial reconciliations of grantees' payments to supporting documentation and its invoice reviews are effective to determine whether costs paid with the grant are allowable and to identify, resolve, and recover costs for which the grantee is unable to provide adequate support.*
- *The Department of Health should recover the overpaid grant amounts.*

⁴ Department of Administration Grants Management Policy 08-10.

Finding 2

The Department of Health did not always comply with state and department grant policies to ensure that it adequately monitored grantees.

The department did not perform the required financial reconciliation for 2 of the 15 grants we tested that exceeded \$50,000. These grantees received \$70,000 and \$153,000, respectively. The department's grant managers for these grants relied on a staff member in the Finance and Facilities Management Division to perform the required financial reconciliations; however, they were unaware that this staff member moved to a different position before performing the reconciliations. State policy requires that agencies perform at least one financial reconciliation of grant expenditures for grants greater than \$50,000.⁵

In addition, the department did not perform the required site visits for 2 of the 13 grants we tested that exceeded \$250,000. A \$405,000 grant with an original effective date from February 21, 2011, to December 31, 2012, with an extension until January 31, 2013, required an annual site visit. The department did not perform the site visit for this grantee until January 25, 2013. The second grant for \$299,735 originally in effect from February 21, 2011, to December 31, 2012, with an extension until March 31, 2013, also required an annual site visit. In this case, the department did not perform the site visit until March 13, 2013. State policy requires that agencies perform one site visit during the grant period for grants greater than \$50,000, and annual site visits for grants exceeding \$250,000.⁶

Finally, the department could not provide evidence that it had obtained all the required progress reports outlined in a \$153,000 grant agreement prior to making further grant payments. The grant agreement required that the grantee provide three semi-annual status reports and a final report; however, the department was only able to provide evidence of one status report in its grant files. State policy prohibits the department from making grant payments when status reports are past due.⁷

Because the department did not adequately monitor these grants, it was unable to ensure that the grantees were using the grant money to accomplish the goals of the grants and to address problems or other issues in a timely manner.

Recommendations

- *The Department of Health should perform financial reconciliations in compliance with policies and procedures.*
- *The Department of Health should conduct monitoring visits of grantees in compliance with applicable policies.*

⁵ Department of Administration Grants Management Policy 08-10.

⁶ Department of Administration Grants Management Policy 08-10.

⁷ Department of Administration Grants Management Policy 08-09.

- *The Department of Health should ensure that grantees comply with all reporting requirements outlined in the grant agreement before making future grant payments.*

The Department of Health paid grantees for costs that were unallowable because the grantee incurred the costs before the start of the grant period.

Finding 3

For 3 of 40 grants we tested, the department reimbursed some grantees for costs that were unallowable because they occurred before the effective date of the grant agreement. The grant agreement stated that the grant was not effective until the later of the date specified in the agreement or when the department obtained the final required signature. The grant agreement prohibited the grantee from performing any work until the department notified the grantee that the grant was effective. According to statute, a grant agreement is not valid and the state is not bound by the grant unless the grant has been fully executed.⁸

The department reimbursed grantees we tested for the following costs which included unallowable costs:

- The department paid a \$13,622 grant invoice covering the period November 1, 2010, through January 31, 2011, for a grant agreement with an effective date of November 29, 2010.
- The department paid a \$1,870 grant invoice covering the period from November 16, 2011, through November 30, 2011, for a grant with an effective date of December 27, 2011. All of this payment was unallowable.
- The department paid a \$23,665 grant invoice for the period October 1, 2011, through December 3, 2011, on a grant with an effective date of November 2, 2011.

Department staff stated that they knew they were paying the grantees for costs incurred before the grants agreement were effective, but believed the payments were acceptable because these grantees generally received grants each year and did not suspend grant-related services while awaiting the execution of the next grant agreements.

Recommendations

- *The Department of Health should only pay for costs that occur during the effective dates of the grant.*
 - *The Department of Health should identify and obtain recovery for costs paid outside the grant period.*
-

Finding 4 **The Department of Health miscategorized certain grant transactions in the state's accounting system.**

The department did not accurately record certain grants in the state's accounting system for fiscal years 2012 and 2013. The department miscoded approximately \$27.5 million of "grants" as "aids" in the state's accounting system. Department staff explained that the miscoding occurred because they had not been clearly instructed on how to correctly code the transactions when the state transitioned to its new accounting system at the beginning of fiscal year 2012.

After initially recording many of the fiscal year 2012 grants, department staff learned that the code they had used to record the grants misclassified the transactions as aids. Because of the miscoding, the department is unable to effectively use information directly from the accounting system.

Recommendation

- *The Department of Health should ensure that it properly codes all grant transactions in the state's accounting system.*
-



Protecting, maintaining and improving the health of all Minnesotans

June 24, 2013

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

Dear Mr. Nobles:

Thank you for the opportunity to respond to your audit report regarding internal controls over the administration and oversight of grants administered by the Department of Health. We are proud of our efforts to implement strong internal controls over grants and your conclusion that our controls were generally adequate to ensure accurate reimbursement of grant expenditures, compliance with finance related legal provisions and accurate recording of expenditures in the state's accounting systems. The following statements describe the corrective actions already taken or that will be taken to address the findings and recommendations in your report.

Finding #1

The Department of Health overpaid approximately \$38,000 to several grantees.

Recommendation

The Department of Health should develop a process that prevents or detects duplicate payments.

Response

The department agrees with this finding and recommendation and will develop a process to prevent or detect duplicate payments by December 31, 2013.

Person Responsible: Sherry Kromschroeder, Financial Services Director, Facilities and Financial Management Division

Recommendation

The Department of Health should ensure that its financial reconciliations of grantees' payments to supporting documentation are effective to determine whether costs paid with the grant are allowable to identify, resolve, and recover costs for which the grantee is unable to provide adequate support.

Response

The department agrees with this recommendation and will provide financial reconciliation and invoice review training to all grants staff by September 30, 2013.

Executive Office • 625 Robert Street North • PO Box 64975 • St. Paul, MN, 55064-0975 • (651) 201-5810 phone

<http://www.health.state.mn.us>

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Persons responsible for training: Alyssa Haugen, Grants Management Coordinator and Amy Jorgenson, Director of Internal Audit

Recommendation

The Department of Health should recover the overpaid grant amounts.

Response

The department partially agrees with this recommendation. For the first two amounts noted in the finding, we will offset future invoices to account for the erroneous double payments. For overpayments resulting from financial reconciliation or invoice reviews, some of the overpayments have already been recovered. For others, the department will recover amounts if the grantee is still in business, it is cost effective to pursue overpayment, and/or the total amount of funds paid exceeded the authorized grant amount. Overpayment on one invoice does not always mean that the department overpaid on the entire grant.

Persons Responsible: Various Grant Managers in MDH, Sherry Kromschroeder, Financial Services Director, Facilities and Financial Management Division.

Finding #2

The Department of Health did not always comply with state and department grant policies to ensure that it adequately monitored grantees.

Recommendation

The Department of Health should perform financial reconciliations in compliance with policies and procedures.

Response

The department agrees with this recommendation. As stated above, the department will conduct financial reconciliation training for grants staff by September 30, 2013. All divisions are now aware of the need to perform financial reconciliations.

Persons responsible for training: Alyssa Haugen, Grants Management Coordinator and Amy Jorgenson, Director of Internal Audit

Recommendation

The Department of Health should conduct monitoring visits of grantees in compliance with applicable policies.

Response

The department agrees with this recommendation. The division that this recommendation pertains to is aware of the requirement and will begin monitoring visits for its grantees. Grant managers will receive periodic reminders and training about best practices for grant monitoring through the department's grant manager workgroup.

Person responsible for reminders and training: Alyssa Haugen, Grants Management Coordinator

Recommendation

The Department of Health should ensure that grantees comply with all reporting requirements outlined in the grant agreement before making future grant payments.

Response

The department agrees with this recommendation and considers it resolved. The division that this recommendation pertains to has taken steps to improve the process for monitoring progress reports and ensuring they are received from grantees in a timely manner before payments are issued.

Finding #3

The Department of Health paid grantees for costs that were unallowable because the grantee incurred the costs before the start of the grant period.

Recommendation:

The Department of Health should only pay for costs that occur during the effective dates of the grant.

Response

The department agrees with this recommendation and will include this topic when conducting financial reconciliation training by September 30, 2013.

Persons responsible for training: Alyssa Haugen, Grants Management Coordinator and Amy Jorgenson, Director of Internal Audit

Recommendation:

The Department of Health should identify and obtain recovery for costs paid outside the grant period.

Response

The department accepts this recommendation; however, we plan to pursue recovery of the costs only in cases where the department did not authorize the services provided.

Finding #4

The Department of Health miscategorized certain grant transactions in the state's accounting system.

Recommendation

The Department of Health should ensure that it properly codes all grant transactions in the state's accounting system.

Response

The department agrees with this recommendation and considers it resolved. Upon internal discovery of this issue in early 2013, employees in the Facilities and Financial Management Division identified all open grants that could be corrected and changed the coding to reflect the proper category of grant in the state's accounting system. Staff also documented and implemented a procedure to ensure the correct code is selected when grants are entered into SWIFT.

Sincerely,

A handwritten signature in black ink, appearing to read "Edward P. Ehlinger". The signature is fluid and cursive, with a long horizontal stroke at the end.

Edward P. Ehlinger, M.D., M.S.P.H.

Commissioner

P.O. Box 64975

St. Paul, MN 55164-0975