Department of Human Services

Financial Audit
Fiscal Year Ended June 30, 1997

March 1998

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Financial Audit Division
Office of the Legislative Auditor
State of Minnesota

98-20

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STATE OF MINNESOTA
OFFICE OF THE LEGISLATIVE AUDITOR
JAMES R. NOBLES, LEGISLATIVE AUDITOR

Senator Deanna Wiener, Chair
Legislative Audit Commission

Members of the Legislative Audit Commission

Mr. David S. Doth, Commissioner
Department of Human Services

We have audited selected aspects of the Department of Human Services for the fiscal year ended June 30, 1997, as further explained in Chapter 1. The work conducted in the department is part of our Statewide Audit of the state of Minnesota's fiscal year 1997 financial statements. The Comprehensive Annual Financial Report for the year ended June 30, 1997, includes our opinion thereon dated December 8, 1997. This was not a complete audit of all financial activities of the Department of Human Services. The following Summary highlights the audit objectives and conclusions. We discuss our concerns more fully in the individual chapters of this report.

We conducted our audit in accordance with generally accepted auditing standards and *Government Auditing Standards*, as issued by the Comptroller General of the United States. Those standards also require that we design the audit to provide reasonable assurance that the Department of Human Services complied with provisions of laws and regulations that are significant to the audit. The management of the Department of Human Services is responsible for establishing and maintaining the internal control structure and compliance with applicable laws, regulations, contracts, and grants.

This report is intended for the information of the Legislative Audit Commission and the management of the Department of Human Services. This restriction is not intended to limit the distribution of this report, which was released as a public document on March 20, 1998.

James R. Nobles
Legislative Auditor

Claudia J. Gudvangen, CPA
Deputy Legislative Auditor

End of Fieldwork: January 29, 1998

Report Signed On: March 13, 1998

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SUMMARY

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Department of Human Services

Financial Audit
For the Fiscal Year Ended June 30, 1997

Public Release Date: March 20, 1998 No. 98-20

Agency Background

The Department of Human Services (DHS) administers a variety of programs that provide financial and medical aid to eligible Minnesotans. The department's commissioner, Mr. David Doth, oversees the administration of nearly $5 billion, including over $2 billion of federal funds, for needy persons. The largest program, Medical Assistance, is the state's Medicaid program. Other aid is provided as cash benefits or food stamps. Administration of these programs in accordance with state and federal regulations is complex and dynamic. The department deals with volumes of federal regulations, interactions with local levels of government, welfare reforms, and changing technology.

Audit Scope and Conclusions

Our audit scope was limited to those activities material to the state of Minnesota's Comprehensive Annual Financial Report or the Single Audit of federal programs for the year ended June 30, 1997. We found that the department fairly presented its financial information in the state's financial report, in accordance with generally accepted accounting procedures. Except as stated below, DHS complied, in all material respects, with the federal requirements governing the programs tested.

We found the following instances of noncompliance with federal regulations for the Medical Assistance program. The department did not accurately report expenditure data to the federal government. DHS did not routinely monitor overrides of certain edits designed to deny medical payments. Also, DHS continued to pay for costly medical procedures without first verifying prior approval. Finally, DHS continued to have an inadequate system of accounting for the Drug Rebate program.

We also found the following instances of noncompliance with other federal requirements. DHS failed to promptly change its federal cash requests for the income maintenance programs as a result of changes in the federal participation rate. In addition, we found that DHS had not fully implemented prior recommendations concerning the processing and accounting for receipts. The department did not have adequate controls to ensure that federal funds were not used to purchase goods or services from entities suspended or debarred by the federal government. Finally, we found that DHS was not current in its review of subrecipients.

In its response to the report, DHS indicated that it agrees with the findings and is implementing corrective action.

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Audit Participation

The following members of the Office of the Legislative Auditor prepared this report:

Claudia Gudvangen, CPA	Deputy Legislative Auditor
Jeanine Leifeld, CPA, CISA	Audit Manager
Cecile Ferkul, CPA, CISA	Auditor-in-Charge
Lori Kloos, CPA	Senior Auditor
Karen Klein, CPA	Senior Auditor
Steve Johnson, CPA	Senior Auditor
Dale Ogren, CPA, CISA	Senior Auditor
Scott Tjomsland	Senior Auditor
Shane Smeby, CPA	Senior Auditor
Connie Stein	Staff Auditor
Rick Weinmeyer	Staff Auditor
Sean Bagan	Intern

Exit Conference

We discussed the findings and recommendations in this report with the following staff of the Department of Human Services on February 27, 1998:

Thomas Moss	Deputy Commissioner
Dennis Erickson	Assistant Commissioner
David Ehrhardt, CPA	Director - Internal Audit
Jon Darling	Director - Financial Management Division

Chapter 1. Introduction

The Department of Human Services (DHS) administers a variety of programs that provide financial and medical aid to eligible Minnesotans. Minnesota Statutes, Chapters 256 through 256G, prescribe the types of aid the state provides and the eligibility criteria. Federal regulations and state plans approved by the federal government also control program activity. Mr. David Doth has been the commissioner of the department since October 1996.

Our audit scope focused on the department's fiscal year 1997 revenues and expenditures shown in Tables 1-1 and 1-2. These financial activities were material to the state's financial statements and to the Single Audit objectives, as explained below.

Table 1-1
Selected Revenue Programs
Fiscal Year 1997

Revenue Area	Amount
Residential Treatment Center Cost of Care	$141,310,151
Medical Provider Surcharge	125,580,315
Chemical Dependency Cost of Care	12,254,640

Source: Derived from the Minnesota Accounting and Procurement System.

Our primary objective is to render an opinion on the state of Minnesota's financial statements included in its Comprehensive Annual Financial Report for fiscal year 1997. This includes determining whether the financial statements of the state fairly present its financial position, results of operations, and changes in cash flows in conformity with generally accepted accounting principles. As part of our work, we gain an understanding of the internal control structure and ascertain whether the state complied with laws and regulations that may have a direct and material effect on its financial statements. The Comprehensive Annual Financial Report for the year ended June 30, 1997, includes our report, issued thereon, dated December 8, 1997.

The Statewide Audit also meets the requirements of the federal Single Audit Act, relating to federal financial assistance. The Single Audit Act establishes two additional audit objectives and requires us to determine:

- Did the state comply with rules and regulations that may have a material effect on each major federal program?

- Did the state have internal control systems to provide reasonable assurance that it managed federal financial assistance programs in compliance with applicable laws and regulations?

We selected audit areas to provide us with the evidence necessary to meet our objectives. Audit areas were selected either because of their financial statement impact or their designation as "major" federal programs.

Our review focused on state level controls over compliance. We did not review and evaluate county level controls established to ensure that DHS made payments only on behalf of eligible recipients.

Table 1-2
Selected Grant Program Expenditures
Fiscal Year 1997

Program Name	Federal	State	Total
Health Care Programs			
Medical Assistance	$1,581,220,456	$1,455,910,746	$3,037,131,202
General Assistance Medical Care	0	152,574,579	152,574,579
MinnesotaCare	0	72,562,979	72,562,979
Income Maintenance Programs			
Family Support (1)	$ 179,110,164	$ 259,501,772	$ 438,611,936
Food Stamps (2)	202,123,540	0	202,123,540
Food Stamps-Administration	29,631,123	4,202,683	33,833,806
General Assistance	0	54,114,958	54,114,958
Minnesota Supplemental Aid	0	62,517,544	62,517,544
Other Grants			
Substance Abuse Preventive Treatment	$ 11,135,433	$ 0	$ 11,135,433
Social Services	39,090,703	0	39,090,703
Community Social Services	0	51,723,388	51,723,388
JOBS/STRIDE	11,526,482	11,227,445	22,753,927
Child Support Enforcement	50,140,689	8,135,213	58,275,902
Consolidated Chemical Dependency Treatment	0	59,600,036	59,600,036

(1) Includes Aid to Families with Dependent Children (AFDC), Special Needs, Emergency Assistance, and the Minnesota Family Investment Program (MFIP).

(2) Includes benefits paid through the state's accounting system ($15,938,698), food stamp coupons distributed by DHS ($99,450,474), and benefits withdrawn electronically by program recipients ($86,734,368).

Source: Derived from the Minnesota Accounting and Procurement System and food stamp records maintained by DHS.

The Minnesota Financial and Compliance Report on Federally Assisted Programs for the year ended June 30, 1997, will include our reports on the supplementary information schedule, internal control structure, and compliance with laws and regulations. We anticipate that the Department of Finance will issue this report in March 1998.

We explain the health care programs in Chapter 2 and the income maintenance programs in Chapter 3. In Chapter 4, we discuss the department's collection, deposit, and recording of various receipts. Chapter 5 describes other DHS grant programs we audited. Finally, in Chapter 6, we highlight other federal compliance issues.

Chapter 2. Medical Assistance and Other Health Care Programs

Chapter Conclusions

The state spent over $3 billion for Medical Assistance, General Assistance Medical Care, and MinnesotaCare during fiscal year 1997. DHS grant expenditures for the health care programs were fairly presented in conformity with generally accepted accounting principles, in all material respects, in the state of Minnesota's financial statements for fiscal year 1997.

In testing the medical assistance program, we found the following instances of noncompliance with applicable federal regulations. The department did not submit accurate Medical Assistance reports to the federal government. Claims processing management did not review reports to monitor overridden edit codes. The department had not verified that costly medical procedures were authorized prior to payment. Finally, the drug rebate unit did not have an accounting system to accurately account for collections. Three of these issues were prior findings that the department had not yet fully implemented.

DHS administers three major health care programs:

- **Medical Assistance** - This is the state's Medicaid Program. The federal government reimburses the state for approximately 54 percent of the Medical Assistance benefit costs.

- **General Assistance Medical Care** - This program extends similar medical benefits to certain people not qualifying for Medical Assistance. This program is entirely state funded.

- **MinnesotaCare** - This is the state's health insurance plan for low income people with no other insurance. The state shares these program costs with the medical community, program participants, and the federal government.

Many features of these programs are similar; the main distinction is the clientele each serves. Table 2-1 shows the fiscal year 1997 program expenditures for these three programs. DHS estimates that these programs serve approximately 545,000 citizens.

Table 2-1
Health Care Programs
Fiscal Year 1997 Expenditures

Program	FY97 Expenditures
Medical Assistance	$3,037,131,202
General Assistance Medical Care	152,574,579
MinnesotaCare	72,562,979
Total	$3,262,268,760

Source: Minnesota Accounting and Procurement System, on an accrual basis.

Audit Scope and Objectives

We had two primary objectives in auditing the health care programs. The first objective was to determine whether expenditures for the programs, as reported on the state's financial statements, were fairly stated in accordance with generally accepted accounting principles. Our second objective, required by the Single Audit Act, was to determine whether the department complied with federal laws and regulations relating to the Medical Assistance Program, and whether the department had internal control systems to provide reasonable assurance that it managed that program in compliance with applicable federal laws and regulations. We obtained an understanding of the design of relevant policies and procedures at the state level and determined whether they have been placed in operation, and we assessed control risk. We did not review and evaluate county level controls established to ensure that DHS made payments only on behalf of eligible recipients. To reach our conclusions, we interviewed various DHS personnel, examined agency documentation, and tested selected transactions.

Health Care Program Administration

Medical Assistance and General Assistance Medical Care are state supervised, county administered programs. The state works in partnership with the 87 counties to provide these benefits. The counties obtain, verify, document, and update information from program applicants to determine their eligibility status. The counties maintain the recipient case files.

DHS must ensure that it makes payments in accordance with the federal regulations for the Medical Assistance Program and in accordance with statutory provisions for the General Assistance Medical Care and MinnesotaCare programs. DHS uses two computer systems to assist with medical program eligibility and claims processing. The MAXIS computer system determines eligibility for the various income maintenance programs and facilitates eligibility determinations for the health care programs. The Medicaid Management Information System (MMIS II) system processes incoming claims for all of the health care programs DHS administers.

Eligibility Determination

Participation in the health care programs starts at the county level, where a potential program participant completes a Combined Application Form. This form gathers data common to many different programs administered by DHS, such as family size and income. The county financial worker enters the information from the Combined Application Form into the MAXIS computer system. MAXIS determines eligibility for the various income maintenance programs, facilitates eligibility determinations for the health care programs, and distributes cash assistance and food stamp benefits. (Chapter 3 provides additional information on the income maintenance programs.) Some of the income maintenance programs automatically qualify recipients for Medical Assistance or another health care program benefits. Over half of health care program participants qualified for these programs due to their participation in income maintenance programs such as Aid to Families with Dependent Children.

If an applicant does not qualify for health care assistance through an income maintenance program, the county worker determines whether the person qualifies for a health care program based on other information. Once the county financial worker determines eligibility on MAXIS, the worker must also enter the eligibility status into the MMIS II system, which is the health care programs' claim processing system. Figure 2-1 shows the major steps used in the eligibility determination process.

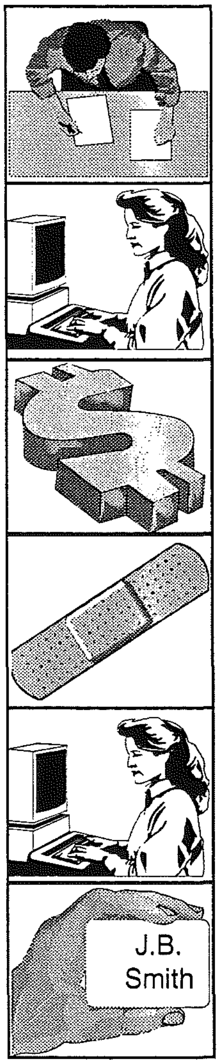
The lack of an automated eligibility interface between MAXIS and MMIS II is a system design weakness that creates the potential for MMIS II to process a medical claim for a recipient who is not eligible for benefits. The department, aware of this weakness, has implemented the following manual controls to prevent, detect, and correct eligibility discrepancies in a timely manner.

- When a county financial worker changes a recipient's eligibility status in MAXIS, the system prompts the county worker to also update the MMIS II eligibility status.

- DHS distributes monthly reports to the counties showing MAXIS and MMIS II eligibility discrepancies. County financial workers must investigate each reported discrepancy and make any appropriate correction. Timely correction of the discrepancies is especially critical for persons enrolled in the managed care plans, where MMIS II automatically generates monthly payments based on client eligibility status.

- The department monitors county financial worker errors to identify county workers that continually generate large numbers of discrepancies. DHS can then provide additional training as needed to improve the financial worker's performance.

**Figure 2-1 Health Care Programs
Eligibility Determination Process**



Applicant completes Combined Application Form and meets with county financial worker to determine eligibility.

County financial worker enters Combined Application Form information into the MAXIS System.

MAXIS determines eligibility for cash assistance programs. Eligibility in cash assistance programs qualifies applicant for medical program.

If applicant is not eligible for cash assistance program, county financial worker uses MAXIS to determine eligibility for medical program only.

County financial worker enters the medical program eligibility status into MMIS II. The eligibility status on MAXIS and MMIS II should be the same.

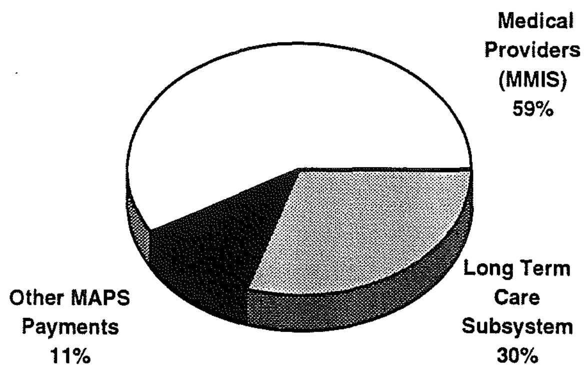
Eligible participant receives a Medical Benefits Card. The participant presents this card when requesting medical services.

Source: Auditor prepared.

Medical Assistance Expenditure Transactions

MMIS II processes all medical service claims. The MMIS II system refers nursing home claims to the long term care subsystem for further processing. These systems feed information to the state's accounting system (MAPS), which ultimately produces all the warrants that pay the claims of the various health care programs. DHS also records other health care program transactions directly onto the MAPS accounting system. Figure 2-2 shows the payments made during fiscal year 1997 through each payment process.

Figure 2-2
Health Care Programs
Fiscal year 1997 Expenditures by Payment Process



Source: Auditor prepared from MAPS expenditure data.

Traditionally, Medical Assistance has been a "fee for service" program. This means that DHS paid medical providers only for specific services at rates set by the program. In an effort to control the rising program costs, the department has been moving recipients into managed care systems In these systems the state pays a set monthly fee to managed care providers for all recipients enrolled in the program, regardless of whether the recipient obtained medical services during the month. In return, the managed care providers agree to provide a range of medical services as needed for the fixed monthly fee.

Medical Provider Payments

DHS uses the MMIS II system to process claims submitted by medical service providers such as doctors, dentists, hospitals, and health maintenance organizations. DHS developed this system in accordance with federal specifications and implemented it in June 1994. MMIS II determines the payment amounts and passes this data to the state's accounting system (MAPS). MAPS uses the data to generate warrants to medical providers and record the transactions as state expenditures. MMIS II issues remittance advises to the medical providers and benefit statements to the recipients of the care. The MMIS II system processed $1,965,360,882 in payments during fiscal year 1997.

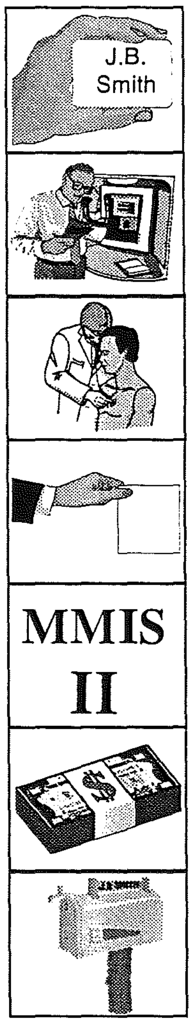
MMIS II has over 900 edits to control claims processing and ensure compliance with intricate federal and state program requirements. DHS designed these edits to ensure that:

- the medical provider has been approved to participate in the program;
- the person receiving the medical benefit is an eligible participant of the program;
- the medical service is reimbursable under the program guidelines;
- the amount reimbursed is in accordance with approved rates; and
- the provider submitted the claim within the appropriate time limit (within a year from when the medical service was provided).

If a medical provider submits a claim that does not meet these criteria, MMIS II either denies the claim or "suspends" it until the staff resolves the problem or denies the claim.

During fiscal year 1997, DHS processed roughly 22 million medical claims. Many claims are for small dollar amounts, such as prescriptions. Other claims are less frequent but for higher dollar amounts, such as in-patient hospital care. Still other claims are for recurring costs, such as monthly managed care payments. Figure 2-3 shows the major steps used for medical claims processing.

Figure 2-3
Health Care Programs
Claims Processing



Program recipient presents Medical Benefits Card to a medical provider.

Medical provider calls the Eligibility Verification System (EVS) to determine the current eligibility status of the recipient. EVS uses MMIS II's eligibility status.

Medical provider gives care to the eligible recipient.

Medical provider submits reimbursement claim to the Department of Human Services.

MMIS II processes claim against recipient, provider, procedure, and rate edits.

MMIS II pays approved medical providers for allowable care given to eligible recipients at authorized rates.

MMIS II notifies recipients of payments made for medical services they received.

Source: Auditor prepared.

Long Term Care Payments

DHS uses its long term care subsystem to make the recurring monthly payments to nursing homes and other long term care facilities for health care program participants. DHS initially inputs the claims into MMIS II, which performs some edit validations. MMIS II then passes these claims to the long term care subsystem for rate verification and payment determination. The long term care subsystem interfaces with the state's MAPS accounting system to produce the payment warrants and to post the transactions to the state's accounting system. The long term care subsystem provides data back to the MMIS II system to update the payment history file. Payments processed through the long term care subsystem during fiscal year 1997 totaled $1,008,686,779, approximately one-third of all health care program expenditures.

Other Health Care Program Payments

As shown in Figure 2-2, DHS processes about 11 percent of all health care program transactions directly through the state's accounting system (MAPS). Table 2-2 shows the most significant of those transactions during fiscal year 1997.

Table 2-2
Other Health Care Program Transactions
Fiscal Year 1997

DHS transferred funds to DHS's regional treatment centers for residents and chemical dependency program participants who are eligible for the health care programs.	$60,339,906
DHS transferred funds to certain medical providers for day training and habilitation services.	$83,767,782
DHS made monthly disproportionate population adjustment payments to the Hennepin County Medical Center and the University of Minnesota hospitals. The payments compensate these hospitals for the high proportion of health care program participants within their caseloads.	$24,240,000
DHS collected and distributed federal administrative aids related to the health care programs. DHS paid some of these aids to the counties to reimburse them for their personnel and related costs necessary to determine eligibility and maintain case files. DHS also reimbursed the state's General Fund for the cost of maintaining the state's accounting, procurement, and personnel/payroll systems. DHS kept some of the aid to offset the cost of maintaining the MAXIS and MMIS II systems and general program administration.	$87,003,334
DHS collected rebates for drugs purchased through the Medical Assistance Program. DHS enters these receipts in MAPS as expenditure reductions offsetting health care expenditures. (See further discussion of the drug rebate program later in this chapter.)	$27,002,859
DHS also collected overpayments made to providers, recoveries from third parties (such as insurance companies or estates), and other types of benefit recoveries. DHS records these receipts in MAPS as revenues credited to the health care programs.	$47,152,055

Source: Auditor analysis of fiscal year 1997 MAPS activities.

System Security

The MAXIS and MMIS II systems run on the state's central mainframe computers. The Department of Administration's InterTechnologies Group (InterTech) operates the mainframe computers and manages the data center. Programmers at the Department of Human Services maintain the system software.

InterTech and the Department of Human Services jointly administer security for the DHS computer systems. A software security package controls access to the state's two central mainframe computers. This software protects against unauthorized destruction, disclosure, modification, or use of data and computer resources. The software acts as an extension to the computer's operating system. It will not permit a user to access data or use a computer resource unless a security officer or the data owner explicitly authorizes that access.

Conclusions

DHS's grant expenditures for the health care programs were fairly presented in accordance with generally accepted accounting principles, in all material respects, in the state of Minnesota's financial statements for fiscal year 1997. Except as explained in Findings 1 through 4, DHS complied, in all material respects, with federal requirements governing the Medical Assistance Program.

1. PRIOR FINDING PARTIALLY RESOLVED: DHS did not accurately complete certain required federal reports.

DHS did not perform reasonable validation procedures to ensure that the Medical Assistance expenditures reported to the federal government were accurate. Fiscal year 1997 was the first year DHS programmed MMIS II to categorize expenditures by service type. DHS developed this MMIS II program to report complete financial information required by the federal government on the quarterly HCFA-64 report. As stated in our prior audit reports, DHS had not been able to provide the federal government with the required information for fiscal years 1995 and 1996.

Beginning in fiscal year 1997, the MMIS II system produced reports which categorized program expenditures into the federally required service types. DHS began reporting these categories to the federal government on the quarterly HCFA-64 reports. It also began restating the quarterly reports for fiscal years 1995 and 1996 using the MMIS II programmed amounts. However, department staff did not analyze the resulting quarterly reports for consistency and reasonableness of the reported data.

We found that, in at least one service type category, the amounts produced by the MMIS II system appear to be inaccurate. In addition, our analysis of the fiscal year 1997 quarterly reports found many other unexpected variances between service type categories from quarter to quarter which DHS program personnel were unable to explain. We believe that these unexplained variances may be indications of other inaccuracies.

Recommendations

- *DHS should verify each category of the HCFA-64 for reasonableness prior to submitting the report to the federal government. DHS should resolve any material discrepancies between expected and reported expenditures.*

- *DHS should review reports for fiscal year 1995, 1996, and 1997 and submit revised HCFA-64 quarterly reports for all quarters with material discrepancies.*

2. DHS did not review edit override reports on a regular basis.

DHS did not use MMIS II reports to review instances where claims processing staff overrode edits designed to deny a payment of a medical claim. The MMIS II system includes many edits designed to ensure compliance with state and federal regulations for the medical programs.

In some cases, a medical provider may protest a claim that MMIS II has previously denied. The provider may resubmit the claim, attaching additional documentation to support the claims legitimacy. Upon review of this additional information, a DHS claims processor may determine that the claim is appropriate and should be paid. The claims processor would then override the applicable MMIS II edit, resulting in payment to the provider. The claims processing unit trains certain claims processors to handle these types of claims. The claims processing manual also includes guidance in making these decisions. Although MMIS II produced reports that identified edit override determinations, DHS did not use the reports to monitor the appropriateness of these transactions.

DHS should monitor edit overrides since they result in payments that MMIS II would normally not allow. It should spot-check override decisions made by claims processors for appropriateness and control purposes. The department should ensure that only properly trained and authorized claims processors perform overrides. It should review the volume and value of payments made as a result of overridden edits.

Recommendation

- *DHS should regularly review edit override reports to ensure that the overrides are appropriate and necessary.*

3. PRIOR FINDING NOT RESOLVED: DHS paid for costly medical procedures without first verifying prior approval.

The MMIS II system does not verify admission certifications before paying certain costly medical claims. DHS requires medical providers to obtain admission certifications before billing certain expensive medical procedures. The purpose of the admission certification is to confirm that the medical care or procedure is necessary and allowable. The State Plan requires these admission certifications. Currently, Blue Cross/Blue Shield performs the "in-patient hospital care" admission certifications for DHS. When Blue Cross/Blue Shield authorizes the care, it issues an admission certification number to the medical provider. DHS requires providers to include these admission certification numbers on claims for these types of services. However, the MMIS II claims processing system pays claims without verifying the authenticity of the admission certification numbers.

We first reported this issue in our fiscal year 1995 audit report. Since that time, DHS has produced reports of paid claims that should have admission certification numbers. However, DHS has not reviewed the claims to determine whether inappropriate payments have occurred nor has it implemented a system to prevent or detect inappropriate payment of future claims.

Recommendations

- *DHS should review the validity of the admission certification numbers on paid claims.*
- *DHS should take appropriate recourse against medical providers who submitted claims with invalid admission certification numbers.*

Drug Rebates

DHS started the Drug Rebate Program as a result of the Omnibus Budget Reconciliation Act of 1990 (OBRA '90). This federal program requires drug labelers to rebate a part of the drug retail price to the Medicaid agencies for drugs purchased through the Medicaid (Medical Assistance) program. The rebates result from the difference between normal retail costs and the negotiated contract prices. Although the drug labelers may not change the negotiated rebate amounts, OBRA '90 does give drug labelers the right to dispute the number of units DHS claims it purchased. Drug rebates offset federal and state medical assistance expenditures. Rebates collected during fiscal year 1997 totaled $27,002,859.

During our review of the drug rebate program, we found the following weakness:

4. PRIOR FINDING NOT RESOLVED: DHS needs to improve their system of accounting for the Drug Rebate Program.

The record keeping of the drug rebate unit was insufficient to allow it to perform all functions necessary for the drug rebate program. The unit maintained spreadsheets to accumulate drug rebate financial data. It received program information from various sources. The MMIS II system provided the unit with the quarterly billable drug rebate amounts. MMIS II calculated these amounts based on paid pharmacy claims during the quarter and the unit rebate amount for each drug sold. The DHS Financial Management Unit recorded the drug rebate collections into the state's accounting system (MAPS). The drug rebate clerk used this MAPS information to post drug rebate collections to spreadsheets. The clerk also posts rebate adjustments and write-offs to the spreadsheets.

The unit staff did not periodically reconcile the spreadsheets to either MMIS II billing amounts or to deposits recorded on MAPS. The clerk adjusted the current and past spreadsheets to reflect retroactive rebate changes.

Also, DHS did not rebill drug labelers for outstanding rebate amounts nor charge interest on past due bills. DHS sent quarterly bills to labelers only for the current quarter and did not include previously billed unpaid amounts. DHS had outstanding rebate billings dating to 1991, the start of the program.

Recommendations

- *DHS should develop or obtain an accounting system for the Drug Rebate Program. The system should allow for:*
  - *periodic verification of the billing and receipt transactions affecting the accounts receivable balances, and*
  - *the identification of all outstanding drug rebate billings and collected amounts.*
- *DHS should bill drug labelers for past due balances and should charge interest on these amounts.*

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Chapter 3. Income Maintenance Programs

Chapter Conclusions

DHS grant expenditures for the income maintenance programs were fairly presented in conformity with generally accepted accounting principles in the state of Minnesota's financial statements for fiscal year 1997. DHS complied, in all material respects, with federal requirements governing the AFDC and food stamp programs.

As shown in Figure 3-1, DHS administers various income maintenance programs designed to provide a base of income to poor and needy residents. These programs include:

Aid to Families with Dependent Children (AFDC) - This federal/state program provides cash payments to qualifying recipients to meet their needs for food, shelter, clothing, and other daily living needs. The program targets funds toward needy families with dependent children and to needy aged, blind, or disabled people. AFDC also provides for short-term emergency assistance. In fiscal year 1998, AFDC will be replaced with the federal government's new block grant, the Temporary Aid to Needy Families (TANF) program.

Minnesota Family Investment Program (MFIP) - DHS developed this program as a pilot project reform of the AFDC program. MFIP focuses on supporting families while making it more profitable to work than to be on welfare. The program provides financial assistance and wage supplements, child care assistance, and employment and training services. The federal government shares the cost of this program with the state. MFIP will form the basis for distributing TANF block grant funds during fiscal year 1998.

General Assistance - This program extends income maintenance benefits to persons not qualifying for AFDC or MFIP. These cash payments meet the basic living needs of certain Minnesota residents who have net income and resources below state limits. The state fully funds this program.

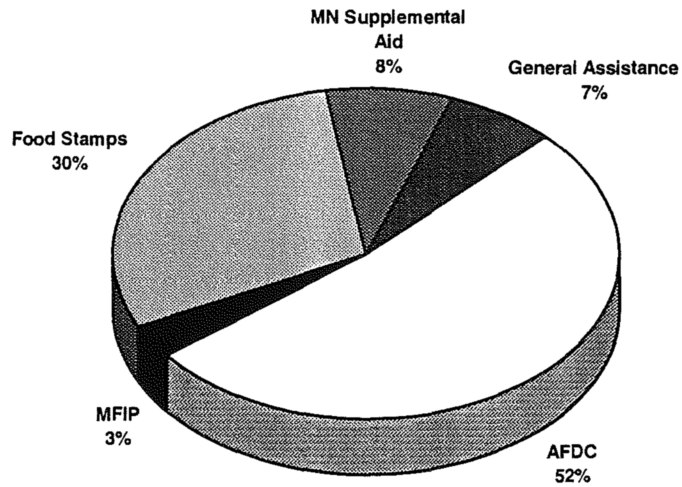
Minnesota Supplemental Aid - This state program works with the federal Supplemental Security Income Program to provide cash benefits to aged, blind, and disabled people who are in financial need.

Food Stamps - Through this program, the federal government hopes to improve the diets of persons living in low-income households by increasing their food purchasing ability. Recipients use their benefits to purchase allowable food products from participating retail stores.

Department of Human Services

The income maintenance programs exceeded $791 million during fiscal year 1997. These costs include the program benefits and the state and county administrative cost. Figure 3-1 allocates this total among the various income maintenance programs.

Figure 3-1
Income Maintenance Programs
Fiscal Year 1997



Source: Analysis of payments through the MAPS accounting system and food stamp coupon disbursements for fiscal year 1997.

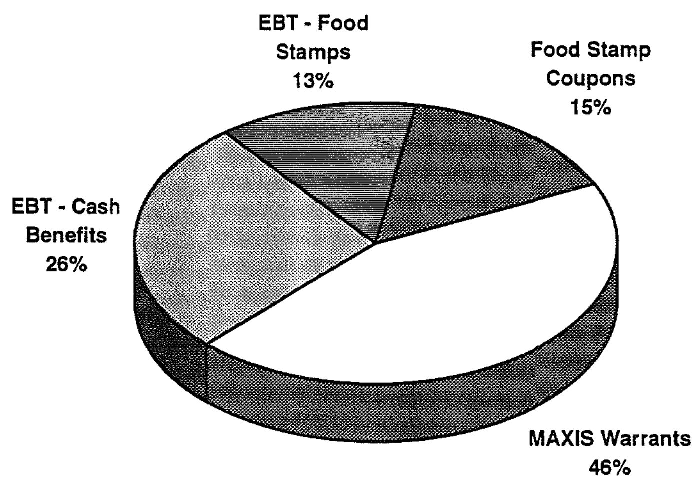
Audit Scope and Objectives

We had two primary objectives in auditing the income maintenance programs. The first objective was to determine whether expenditures for the programs, as reported on the state's financial statements, were fairly stated in compliance with generally accepted accounting principles. Our second objective, required by the Single Audit Act, was to determine whether the department complied with rules and regulations relating to the AFDC (including MFIP) and the food stamp programs, and whether the department had internal control systems to provide reasonable assurance that it managed those programs in compliance with applicable federal laws and regulations. We obtained an understanding of the design of relevant policies and procedures at the state level, determined whether they have been placed in operation, and we assessed control risk. We did not review and evaluate county level controls established to ensure that DHS made payments only to eligible recipients. To reach our conclusions, we interviewed various DHS personnel, examined agency documentation, and tested selected transactions.

Income Maintenance Program Administration

DHS uses three methods to provide income maintenance benefits to recipients. DHS has traditionally used two of these methods, state warrants and food stamp coupons, to provide these entitlement aids to qualified recipients. In recent years, recipients have also been able to access their benefits electronically through automatic teller machines or point of sale machines at retail stores. Originally available only in Hennepin and Ramsey counties, DHS is phasing in electronic benefit transfer (EBT) transactions statewide and intends to use it to virtually replace the traditional methods of providing benefits. Figure 3-2 shows the income maintenance transactions paid through each process during fiscal year 1997.

Figure 3-2
Income Maintenance Programs
Benefit Distribution Methods



Source: Auditor created from MAPS expenditure and food stamp disbursement data.

Warrants and Coupons

DHS uses the MAXIS computer system to accumulate recipient data and calculate the income maintenance benefits available to recipients. Following the process outlined in the first four steps of Figure 2-1, county financial workers enter recipient data into MAXIS from the Combined Application Form. The MAXIS system uses this data to determine the programs that the recipient qualifies for and the amount of aid the recipient is eligible to receive. The MAXIS system then sends payment data to the department's Issuance Operations Center.

The Issuance Operations Center controls the distribution of both warrants and food stamp coupons for income maintenance recipients. The Issuance Operations Center prints and mails state warrants for the income maintenance programs. MAXIS authorizes most benefits at the beginning of each month. The payments made on most other days of the month are for recipients just entering the programs who are not yet on a monthly payment cycle.

DHS distributes food stamp coupons to program recipients who do not receive their benefits electronically. The Issuance Operation Center maintains inventory records showing additions to and withdrawals from the inventory of food stamp coupons. The state receives its stock of food stamp coupons from the federal government and uses the MAXIS system, interacting with the Issuance Operations Center, to distribute the coupons through the mail. The federal government redeems food stamps directly with the vendors. The federal government fully funds the food stamp benefit costs. Fiscal year 1997 expenditures of food stamps coupons totaled $99,450,474.

Electronic Benefit Transfer (EBT) Transactions

Many income maintenance program recipients obtain benefits (including food stamp benefits) through point of sale machines located at grocery stores or automatic teller machines. Recipients receive debit cards and can withdraw benefits when they need them. The department believes that this process helps residents safeguard their benefits, yet still allows continuous access to the benefits. DHS is expanding the availability of electronic benefits statewide. During fiscal year 1997, income maintenance recipients electronically accessed cash benefits totaling $176,013,120 and food stamp benefits totaling $86,734,368.

DHS contracts with a private vendor to process electronic benefit transactions. The MAXIS system provides the vendor with benefit availability data on a daily basis. Likewise, the vendor reports all EBT transactions to DHS daily. These reports are the basis for a wire transfer to reimburse the vendor for the withdrawals and the basis for MAPS expenditure input. The federal government directly reimburses the vendor for electronic food stamp withdrawals. DHS does not record electronic food stamp benefits on MAPS since no cash flows through the state's system. (Some of these processes changed when DHS contracted with a new vendor in June 1997.)

Conclusions

DHS's grant expenditures for the income maintenance programs were fairly presented in accordance with generally accepted accounting principles, in all material respects, in the state of Minnesota's financial statements for fiscal year 1997. DHS complied, in all material respects, with federal requirements governing the AFDC and food stamp programs.

Chapter 4. Selected Departmental Revenues

Chapter Conclusions

DHS's federal revenues, medical provider surcharges, and regional treatment cost of care revenues were fairly presented in conformity with generally accepted accounting principles, in all material respects, in the state of Minnesota's financial statements for fiscal year 1997.

DHS generally complied with federal requirements for cash management. We found, however, that they did not change the AFDC federal participation rate for electronic benefits in a timely manner.

We found internal control weaknesses in DHS's processing and accounting for receipts. The department did not adequately safeguard receipts in the mailroom nor endorse or deposit receipts timely.

Audit Scope and Objectives

We had two primary objectives in auditing the revenue areas listed in Table 4-1. The first objective was to determine whether the revenues, as reported on the state's financial statements, were fairly stated in accordance with generally accepted accounting principles. Our second objective was to determine whether DHS complied with the cash management provisions of the Single Audit Act, and whether the department had internal control systems to provide reasonable assurance that it managed federal cash in compliance with applicable laws and regulations. We also examined DHS's process to record and deposit centrally collected receipts, including receipts from drug rebates, recoveries from third parties, health care program fees and refunds, and medical provider surcharges. To reach our conclusions, we interviewed department employees, reviewed applicable policies and procedures, and observed the department's processes and controls.

Conclusions

The revenues shown on Table 4-1 were fairly presented in accordance with generally accepted accounting principles, in all material respects, in the state of Minnesota's financial statements for fiscal year 1997. However, DHS did not change the AFDC federal reimbursement rate used by the electronic benefits vendor, resulting in some federal funds being requested too early. In addition, the department did not adequately safeguard receipts nor deposit all receipts timely.

Table 4-1
Material Revenue Areas
Fiscal Year 1997

Type of Revenue	Amount
Federal Revenue	
Health Care Programs	$1,581,220,456
Income Maintenance Programs	179,110,164
Food Stamps	231,754,663
Other Major Federal Programs	111,893,307
Medical Provider Surcharges	125,580,315
Regional Treatment Center (RTC) Cost of Care	141,310,151
RTC Chemical Dependency Cost of Care	12,254,640

Sources: Federal financial schedules and the state of Minnesota's financial statements for fiscal year 1997.

Federal Revenue

The federal government provides funding for a portion of many of the programs DHS administers. Often, the program bases the rate of federal participation on a percentage of the total program costs. These federal participation rates typically change on October 1, at the start of the federal fiscal year.

5. **PRIOR FINDING NOT RESOLVED: DHS did not change the AFDC federal reimbursement rate used by the electronic benefits vendor, resulting in federal funds being drawn too early.**

DHS bases its request for federal reimbursement for AFDC benefits provided electronically (EBT benefits) on a daily report it receives from the EBT service vendor. The daily report identifies EBT disbursements by program and allocates them to the federal and state funding sources. On October 1, 1996, the vendor should have changed the federal participation rate for the AFDC program to 53.60 percent. Instead, the vendor continued to allocate AFDC EBT disbursements at the old participating rate of 53.93 percent until February 1997. We estimate that this error resulted in DHS requesting approximately $149,000 of federal funds too early. DHS identified and corrected the overdraw during the year end reconciling procedures. DHS failed to detect a similar error in fiscal year 1996.

Recommendation

- *DHS should verify that it uses the proper federal reimbursement rates to request federal funds.*

Cost of Care Revenues

The seven DHS regional treatment centers, two state nursing homes, and numerous other state operated community based programs collect revenues for the cost of care provided by those facilities. Each state facility is responsible for collecting and depositing these cost of care receipts. Many of the facility residents are participants in the Medical Assistance program. Their care is paid directly by the Medical Assistance program to the facility cost of care accounts through interdepartmental payments. Other sources of cost of care revenue are insurance policies and private payments.

Chemical Dependency Treatment Cost of Care Revenue

State statutes authorize the state's regional treatment centers to operate chemical dependency treatment programs that compete with private sector treatment facilities. Persons treated at the facilities are often placed there by the counties to comply with a court order. The cost of chemical dependency treatment at these state facilities is often paid with funds from the state's Consolidated Chemical Dependency Treatment Fund, which we describe in Chapter 5. During fiscal year 1997, receipts from the Chemical Dependency Treatment Fund comprised 85 percent of the state's chemical dependency cost of care revenue. Total revenue for the chemical dependency treatment facilities during fiscal year 1997 exceeded $12 million.

Medical Surcharge Payments

Medical providers, including hospitals and nursing homes, who wish to conduct business in Minnesota, must make certain surcharge payments to the state. DHS deposits all of these receipts into the state's General Fund. For fiscal year 1997, medical surcharge receipts and other receipts from hospitals totaled $125,580,315.

Medical providers, including physicians, hospitals, nursing homes, and health maintenance organizations, must pay a surcharge to DHS on an annual or monthly basis. Statutes require physicians to pay a $400 annual surcharge at the time they renew their licenses. Nursing homes annually pay $625 per licensed bed as a surcharge. The statutes require hospitals and health maintenance organizations to pay a certain percentage of their net patient revenues or premium payments.

In addition to these surcharges, the statutes also require certain government run hospitals and nursing homes to make additional payments to the state. During fiscal year 1997, the University of Minnesota Hospital and the Hennepin County Medical Center paid the state a total of $2,000,000 per month. Nursing homes operated by certain counties pay the state $5,723 per bed on an annual basis.

Department Receipt Process

DHS receives many of its non-federal receipts through the mail. Each morning the DHS mailroom staff sorts envelopes containing receipts from the department's regular mail based on coding on the envelopes. The mailroom staff delivers the envelopes containing receipts to the DHS cashiers. The cashiers post the receipts to the appropriate accounting systems and then prepare the deposits.

In our fiscal year 1996 audit report, we recommended that DHS improve its receipt process. Some of the improvements that DHS has made include the use of a locked cart to deliver mail from the mailroom to the cashier, the purchase of an automated mail extraction machine, and an automated receipt encoder machine. This equipment minimizes physical contact with the receipts and speeds processing. We continue to be concerned, however, with certain issues relating to the department's receipt processing, as explained below:

6. PRIOR FINDING PARTIALLY RESOLVED: The department did not adequately safeguard receipts nor deposit all receipts timely.

DHS did not adequately safeguard its receipts and delayed depositing of receipts for posting purposes. The mailroom staff did not keep receipts in a secure area prior to delivery to the cashier. Mailroom staff kept receipts in an unlocked drawer. The current DHS mailroom is not physically secure.

The DHS cashiers did not endorse or deposit the receipts until posting to the various accounting systems was completed. By promptly endorsing receipts the department limits the ability to improperly negotiate the receipt. DHS's delay in depositing the receipts until after posting increases the risk of loss or theft. Minn. Stat. Section 16A.275 require that an agency deposit receipts totaling $250 or more in the state treasury daily. This requirement allows the state to maximize its investment earnings and minimizes the risk of loss or theft.

Recommendations

- *DHS should adequately safeguard receipts in the mailroom.*
- *DHS should promptly endorse and deposit receipts in compliance with state statutes.*

Chapter 5. Other Grant Programs

Chapter Conclusions

DHS expenditures for Consolidated Chemical Dependency Treatment, federal Title IV-D Child Support Recoveries, Community Social Service Grants and federal Social Service Block Grants were fairly presented in accordance with generally accepted accounting principles, in all material respects, in the state of Minnesota's financial statements for fiscal year 1997. DHS complied, in all material respects, with federal requirements governing the major federal programs discussed in this chapter.

In addition to the health care and income maintenance programs discussed in Chapters 2 and 3, DHS administers many other federal and state grant programs. Some of these programs are significant enough to be material to the state's financial statements. Others exceed the $10 million threshold that the Federal Single Audit Act defines as a major federal program for the state of Minnesota. Table 5-1 lists other DHS grant programs that we audited for fiscal year 1997.

Table 5-1
Other Grant Programs
Fiscal Year 1997 Federal and State Expenditures

Program	FY97 Expenditures	Audit Coverage: Financial Statement	Single Audit
Consolidated Chemical Dependency Treatment	$59,600,036	√	
Child Support IV-D Grants	$58,275,902	√	√
Community Social Services	$51,723,388	√	
Social Service Block Grants (Title XX)	$39,090,703	√	√
JOBS/STRIDE	$22,753,927		√
Substance Abuse	$11,135,433		√

Sources: Federal financial schedules and the state of Minnesota's financial statements for fiscal year 1997.

Audit Scope and Objectives

We had two primary objectives in auditing these other grant areas. The first objective was to determine whether the expenditures of these programs were fairly stated in accordance with generally accepted accounting principles in the state's financial statements for fiscal year 1997. Our second objective was to determine whether DHS complied with provisions of the Single Audit Act, and whether the department had internal control systems to provide reasonable assurance that it monitored compliance with applicable laws and regulations.

For each of these programs, we obtained an understanding of the design of relevant policies and procedures at the state level, determined whether they have been placed in operation, and we assessed control risk. To reach our conclusions, we interviewed various DHS personnel, examined agency documentation, and tested selected transactions. The remainder of this chapter discusses each of these material programs.

Consolidated Chemical Dependency Treatment Fund - The Consolidated Chemical Dependency Treatment Fund combines revenue from various sources and uses those funds to reimburse chemical dependency treatment centers for care provided to eligible recipients. The fund receives money from three main sources. It receives funding from the federal government through the Federal Substance Abuse Grant. It also receives reimbursements from the state's health care programs (Medical Assistance, General Assistance Medical Care, and MinnesotaCare) for chemical dependency care provided to program recipients. Finally, program policies require counties to reimburse the fund for 15 percent of chemical dependency treatment expenditures made for residents of their counties.

Although the state makes the payments to providers of chemical dependency treatment, the counties determine recipient eligibility and approve provider invoices for payment. DHS maintains a computer system that processes approved provider invoices. This system interfaces with the state's accounting system to produce payments and post summary accounting entries.

Child Support Enforcement Services - Title IV-D Grants - This federal grant program reimbursed the state and counties for costs associated with the enforcement of child support orders and the collection of child support due from non-custodial parents. This program requires DHS to administer county and state level services to locate absent parents, to establish paternity, and to enforce support obligations. Participants of the AFDC, Medicaid, and certain other federal programs must assign their support rights to the state, offsetting program costs.

The federal government participates in the program's costs at various rates. Support enforcement involves both state and county level services. All of Minnesota's 87 counties collected and disbursed child support funds and, therefore, were eligible for administrative cost reimbursement.

Program operating costs increased from a fiscal year 1996 total of $51 million to a fiscal year 1997 total of $58 million. Increased fiscal year 1997 program costs were due to the development of a new child support collection system, which became operational in October 1997. This system centralized the child support collection process, accumulating data in one accounting system rather than at the county level. In the future, the state will also be the central depository for child support collection receipts.

Community Social Service Act State Grants - This is a state program for counties to provide community social services. This program operates in conjunction with the Federal Social Service Block Grant program, discussed below. The county board is responsible for administration, planning, and funding of community social services. Each county must prepare a social services plan, that it updates biennially. Counties must submit a county board approved plan to DHS to receive the state block grant funds.

Department of Human Services

DHS distributes state community social service grants to counties. To receive reimbursement for expenditures, the counties must submit to DHS a financial accounting of expenditures on a quarterly basis. DHS distributes the funds to the counties based on the average monthly county caseloads for AFDC, general assistance, and medical assistance, the number of persons residing in the county, and the number of county residents who are 65 years old or older. During fiscal year 1997, DHS distributed approximately $52 million to the counties under the Community Social Service Act state grant program.

Social Service Block Grants - Title XX - Federal Social Service Block Grants provide funding to states for many social programs. The state, in turn, distributes the funds to the counties. This program operates in conjunction with the state community social service program discussed above. Counties must submit a county board approved plan to DHS to receive the block grant funds. To receive reimbursement for expenditures, the counties must submit to DHS a financial accounting of expenditures on a quarterly basis. DHS distributes block grant money to the counties following the same formula as the state community social service grants. During fiscal year 1997, DHS distributed approximately $39 million in federal funds to counties under the Social Service Block Grant program.

JOBS/STRIDE Grants - This is a federal and state grant program to the counties. A state agency, as a condition of participation in the AFDC program, must operate a JOBS/STRIDE program. The JOBS/STRIDE program assures that needy families with children obtain the education, training, and employment that will help avoid long-term welfare dependence. For this program, the counties serve as the main contact with the program recipients. The counties meet with the recipients and determine recipient needs and eligibility. DHS pays the counties four advance payments and a final settlement payment. Federal and state expense participation for fiscal year 1997 totaled approximately $11.5 million and $11.2 million, respectively.

For fiscal year 1998, the federal government has incorporated the JOBS/STRIDE program into the Temporary Aid for Needy Families (TANF) program, described in Chapter 3.

Substance Abuse Block Grant - The federal government provides these funds to assist states in the treatment and rehabilitation of alcohol and drug abusers. In addition to treatment programs, the federal government has designated some of the block grant funds for prevention programs and specific populations. DHS used $6.7 million of this grant to directly reimburse providers of substance abuse treatment. DHS also paid $5.2 million from this grant into the state's Consolidated Chemical Dependency Treatment Fund, which we discussed earlier in this chapter.

Conclusions

Grant expenditures for Consolidated Chemical Dependency Treatment, federal Title IV-D Child Support Recoveries, Community Social Services grants and the Social Service Block Grant were fairly presented in conformity with generally accepted accounting principles, in all material respects, in the state of Minnesota's financial statements for fiscal year 1997.

DHS complied, in all material respects, with federal requirements governing the Child Support Enforcement IV-D, Social Services Block, JOBS/STRIDE, the Substance Abuse Prevention and Treatment grant programs.

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Chapter 6. Other Federal Compliance Issues

Chapter Conclusions

During our review of federal compliance, we noted two additional instances where DHS did not comply with federal rules and regulations. These instances related to federal suspension and debarment procedures and federal regulations relating to subrecipient monitoring.

The federal government mandates various policies and procedures to states receiving federal aid. We found that DHS was not complying with federal regulations relating to federal suspension and debarment and relating to subrecipient monitoring.

Suspension and Debarment

Federal Regulation 45CFR92.35 prohibits the state from purchasing items with federal money from vendors who have been suspended or debarred by the federal government. Vendors are suspended or debarred when the federal government determines, or is informed, that the vendors have abused the public trust, perhaps by violating program provisions. The federal government expects every state to know who the suspended and debarred vendors are and to have a process in place to prevent them from receiving federal funds.

The large majority of the federal dollars spent by the department were paid either through the MMIS II system, which is used for Medical Assistance payments to medical service providers (refer to Chapter 2), or the MAXIS system, which is used to provide income maintenance benefits (refer to Chapter 3). The department also expended other federal funds directly through the state's MAPS accounting system.

When we examined this issue at the Department of Human Services, we found that the department had a process in place to prevent payment through the MMIS II system. Federal regulations do not apply the prohibition to recipients of the income maintenance programs, so the MAXIS system is exempt from these provisions. We found, however, the following weakness related to payments the department made through the state's accounting system.

7. The department did not have a process to determine whether a potential vendor is suspended or debarred by the federal government prior to obligating federal funds.

Department purchasing personnel were not aware of the federal restrictions related to the payment of federal funds to suspended or debarred vendors. They did not know that the federal government publishes a quarterly list of suspended or debarred vendors. The department was not aware that the federal government requires them to obtain a certification from vendors awarded contracts of $100,000 or more, and we were unable to find any such certifications on file at the department.

Recommendation

- *The department should ensure that federal funds are not being paid to vendors who are suspended or debarred by the federal government.*

Subrecipient Monitoring

Federal regulations require pass through entities to monitor that subrecipients of federal assistance comply with federal program policies. DHS is a pass through entity for many programs they administer. For example, DHS passes federal administrative aids through to the county level to reimburse them for the cost of administering the medical assistance, income maintenance, and child support recovery programs. DHS also passes federal funds through to other types of entities, such as Indian governments or local community groups. We found the following weakness with the department's monitoring of subrecipient compliance with federal regulations:

8. DHS was not timely in its review of subrecipient audit reports.

DHS did not review subrecipient audit reports on a timely basis. The federal government requires certain subgrantees, based on the materiality of the funds they receive, to have a federal compliance audit in conjunction with their financial statement audit. DHS's subgrantees submit the audit reports to the department. DHS then has the responsibility to review the reports, determine whether there are any instances of noncompliance with federal policies, and to monitor and ensure that corrective action is taken to correct the weakness. The Department of Finance has a policy that requires that the subrecipient's corrective action is taken within six months after the department receives the audit report. DHS placed the responsibility for the review of audit reports and the monitoring of corrective action with their internal audit unit.

The department has received 97 percent of the subrecipient audit reports for calendar year 1995 and 63 percent of the reports for 1996. However, they have reviewed only 31 percent of the 1995 reports and 4 percent of the 1996 reports.

Recommendation

- *To ensure compliance with federal regulations and state policy, the department needs to review the subrecipient reports in a more timely manner.*

Status of Prior Audit Issues As of January 29, 1998

May 7, 1997, Legislative Audit Report 97-25 examined the DHS activities and programs material to the State of Minnesota's Annual Financial Report or the Single Audit for the year ended June 30, 1996. The scope included the administration of the state's Medical Assistance and other health care programs, the various income maintenance programs, and other federal and state programs.

In the fiscal year 1996 report, we identified four instances of noncompliance in the Medical Assistance program. We repeated three of these issues in our fiscal year 1997 report. We found that the department had not accurately complete certain required federal reports. Although the department completed the reports for fiscal year 1997, we question the reliability of the data contained in those reports (current Finding 1). The department also had not conducted reviews of certain costly medical procedures to ensure that the procedures had been properly authorized. We found that these reviews were still not being completed during fiscal year 1997 (current Finding 3). In addition, the department had not accurately accounted for its drug rebate accounts receivable or collected drug rebates in accordance with the federal drug contract. Although the department explored various changes to its drug rebate accounting system, it had not substantially implemented the recommendations (current Finding 4). We reported in the fiscal year 1996 report that the department had paid some medical claims that were beyond the federal government's one year limit. We did not find instances of noncompliance with this restriction during fiscal year 1997.

We had also noted weaknesses in DHS's internal controls over the health care programs in the fiscal year 1996 report. DHS had overpaid a provider approximately $6.2 million, due to an error in the MMIS II manual pricing logic. DHS implemented our recommendations by changing the pricing logic related to this particular edit and executing procedures to detect similar errors should they occur.

Finally, we had reported that DHS had not complied with the federal cash management provisions for the Medical Assistance program. DHS changed its procedures to comply with the federal cash draw provisions, allowing the state to maximize its investment income. DHS also had not changed the federal participating rate for a part of the income maintenance programs. DHS made the same error in the current audit (current Finding 5). In addition, DHS had significant weaknesses in their processing and accounting for receipts. Although, the department has made some changes in their receipt processing and safeguarding procedures, weaknesses still exist (current Finding 6).

State of Minnesota Audit Follow-Up Process

The Department of Finance, on behalf of the Governor, maintains a quarterly process for following up issues cited in financial audit reports issued by the Legislative Auditor. The process consists of an exchange of written correspondence that documents the status of audit findings. The follow-up process continues until Finance is satisfied that the issues have been resolved. It covers entities headed by gubernatorial appointees, including most state agencies, boards, commissions, and Minnesota state colleges and universities. It is not applied to audits of the University and quasi-state organizations, such as the metropolitan agencies or the State Agricultural Society, the state constitutional officers, or the judicial branch.

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Minnesota Department of **Human Services**

March 10, 1998

James R. Nobles
Legislative Auditor
Centennial Office Building
658 Cedar Street
St. Paul, MN 55155

Dear Mr. Nobles:

The enclosed material is the Department of Human Services response to the findings and recommendations included in the draft audit report of the financial and compliance audit conducted by your office for the year ended June 30, 1997. It is our understanding that our response will be published in the Office of the Legislative Auditor's final audit report.

The Department of Human Services policy is to follow-up on all audit findings to evaluate the progress being made to resolve them. Progress is monitored until full resolution has occurred. If you have any further questions, please contact David Ehrhardt, Internal Audit Director, at (612) 282-9996.

Sincerely,

Thomas L. Moss

for David S. Doth
Commissioner

Enclosure

cc: Jeanine Leifeld
Cecile M. Ferkul

Department of Human Services
Responses to the Legislative Audit Report
For the Year Ended June 30, 1997

<u>Audit Finding #1</u>

PRIOR FINDING PARTIALLY RESOLVED: DHS did not accurately complete certain required federal reports.

<u>Audit Recommendation #1-1</u>

DHS should verify each category of the HCFA-64 for reasonableness prior to submitting the report to the federal government. DHS should resolve any material discrepancies between expected and report expenditures.

Department Response #1-1

The finding is accurate with regard to specific service categories relating to the counting of family planing services. The department has an ad hoc team of policy and technical staff that meet when the need arises to review problems in the reporting system.

Person Responsible: Dan Schivone, Director, Health Care Systems Development Division

Estimated Completion Date: June 30, 1998

<u>Audit Recommendation #1-2</u>

DHS should review reports for fiscal years 1995, 1996, and 1997 and submit revised HCFA-64 quarterly reports for all quarters with material discrepancies.

Department Response #1-2

The department agrees with the recommendation and, if needed, will revise the appropriate HCFA-64 report.

Person Responsible: Dan Schivone, Director, Health Care Systems Development Division

Estimated Completion Date: June 30, 1998

Department of Human Services
Responses to the Legislative Audit Report
For the Year Ended June 30, 1997

<u>Audit Finding #2</u>

DHS did not review edit override reports on a regular basis.

<u>Audit Recommendation #2</u>

DHS should regularly review edit override reports to ensure that the overrides are appropriate and necessary.

Department Response #2

The department agrees with the recommendation. On February 23, 1998, the department incorporated a review of the appropriate management reports in our daily administrative routine.

Person Responsible: Larry Woods, Director, Health Care Operations Division

Estimated Completion Date: Completed

<u>Audit Finding #3</u>

PRIOR FINDING NOT RESOLVED: DHS paid for costly medical procedures without first verifying prior approval.

<u>Audit Recommendation #3-1</u>

DHS should review the validity of the admission certification numbers on paid claims.

Department Response #3-1

DHS agrees with the recommendation. The DHS Admission Certification Program requires providers of inpatient hospital services to obtain admission certification prior to billing for the services. The DHS medical review agent (MRA) screens admissions for medical necessity via a phone-in system and verifies admission certification or denial by letter. The MRA is required to perform retrospective reviews of approximately 20,000 paid claims per year. These reviews include comparing the information provided over the phone to the medical record to ensure accuracy and medical necessity. As part of the review, the MRA verifies the admission certification number. The DHS contract with the MRA also stipulates that retrospective medical record reviews are to be performed on 100% of transfers and readmissions, 100% of psychiatric admissions, 100% of obstetric admissions without delivery, 100% of out-of-state admissions, and 100% of outlier, short stay and long stay admissions (>59 days). These areas were selected by DHS for review because there is more potential for discrepancies as more denials occur within them.

Inpatient admissions of pregnant women who deliver during the admission and their newborns are not required to be certified because medical necessity is evident. The number of claims for these admissions fluctuates as a result of eligibility policy changes and expansion of managed care, and ranges between 30% and 40% of total claims in the years 1990 to 1995.

Most claims for admissions that require prior authorization such as transplants and investigative surgical procedures are checked against the prior authorization subsystem (both MMIS I and MMIS II), therefore editing for admission certification would be unnecessary. Also, claims for inpatient dental procedures and admissions approved by Medicare are not required to have admission certification numbers.

Between the claims reviewed by the MRA and the claims described above, we can account for 60% and 70% of total claims processed. Therefore, only 30% to 40% of inpatient claims are actually unverified and they are the types of claims with which we have experienced the least amount of discrepancies.

Person Responsible: Paul Olson, Director, Payment Policy Division

Estimated Completion Date: September 30, 1998

<u>Audit Recommendation #3-2</u>

DHS should take appropriate recourse against medical provider who submitted claims with invalid admission certification numbers.

Department Response #3-2

We agree with the recommendation. See Department Response #3-1 for our general comments.

Person Responsible: Paul Olson, Director, Payment Policy Division

Estimated Completion Date: September 30, 1998

Audit Finding #4

PRIOR FINDING NOT RESOLVED: DHS needs to improve their system of accounting for the Drug Rebate Program.

Audit Recommendation #4-1

DHS should develop or obtain an accounting system for the Drug Rebate Program. The system should allow for periodic verification of the billing and receipt transactions affecting the accounts receivable balances and the identification of all outstanding drug rebate billings and collected amounts.

Department Response #4-1

The department agrees with the recommendation. We are in the process to purchase a drug rebate accounting system which will interface with the state's accounting system and generate invoices to include past due amounts.

Person Responsible: Larry Woods, Director, Health Care Operations Division

Estimated Completion Date: September 30, 1998

Audit Recommendation #4-2

DHS should bill drug labelers for past due balances and should charge interest on these amounts.

Department Response #4-2

The department agrees with the recommendation.

Person Responsible: Larry Woods, Director, Health Care Operations Division

Estimated Completion Date: September 30, 1998

Audit Finding #5

PRIOR FINDING NOT RESOLVED: DHS did not change the AFDC federal reimbursement rate used by the electronic benefits vendor, resulting in federal funds being drawn too early.

Audit Recommendation #5

DHS should verify that it uses the proper federal reimbursement rates to request federal funds.

Department Response #5

The department agrees with the recommendation. Our year end reconciliation process detected the error and we reported it to the Legislative Auditor. We were disappointed that our initial attempt at fixing the problem last year was not successful. We have implemented modifications to our accounting procedures to resolve this issue.

Person Responsible: Jon Darling, Director, Financial Management Division

Estimated Completion Date: Completed

Audit Finding #6

PRIOR FINDING PARTIALLY RESOLVED: The department did not adequately safeguard receipts nor deposit all receipts timely.

Audit Recommendation #6-1

DHS should adequately safeguard receipts in the mailroom.

Department Response #6-1

The department agrees with the recommendation. Effective February 26, 1998, the mailroom staff will lock the doors after the post office has delivered the mail to the mailroom. The doors will remain locked until the receipts are sorted and locked in the lock cart used for transporting the receipts to the DHS cashier.

Once the receipting section is relocated to the new secured building, the mail will be directly sent to the DHS cashier from the Post Office by a courier and this will no longer be an issue in the building at 444 Lafayette Road.

Person Responsible: Ron Lang, Director, Management Services Division

Estimated Completion Date: Completed

Audit Recommendation #6-2

DHS should promptly endorse and deposit receipts in compliance with state statutes.

Department Response #6-2

The department agrees with the recommendation. We realized from the initial FY 1996 audit finding that the auditor's original recommendation could not be completely resolved until a new automated receipting process was developed and operational, and the receipting function was relocated to a secure setting. Progress in completely resolving the issue has been substantial and we are on track to achieve complete resolution. There can be a conflict between receipts security and prompt deposit. The Legislative Auditor's recommendation that checks be endorsed immediately upon receipt requires extra time and thus hinders prompt identification and deposit. While DHS uses the "manual deposit method" endorsement of checks prior to deposit will not allow for prompt and accurate deposit. This problem will be resolved when the Automated Receipt Processing system is operational. In the interim we will explore and utilize those methods of receipts processing which achieve the optimum balance between security and promptness.

Person Responsible: Jon Darling, Director, Financial Management Division

Estimated Completion Date: October 31, 1998

Audit Finding #7

The department did not have a process to determine whether a potential vendor is suspended or debarred by the federal government prior to obligating federal funds.

Audit Recommendation #7

The department should ensure that federal funds are not being paid to vendors who are suspended or debarred by the federal government.

Department Response #7

The department agrees with this recommendation. The department wasn't aware of the need for written vendor certification for contracts of $100,000 or more. We will implement certification procedures by September 30, 1998.

We believe that it is the responsibility of the Department of Finance and/or Department of Administration to determine if a vendor has been debarred or suspended since they control the statewide accounting's vendor list for all state agencies. It would not be efficient for a single state agency to examine the federal government's debarred list each time they purchase goods or services from a vendor. We have discussed the problem with the Department of Administration and they have recently established procedures to review the federal list on a monthly basis to adjust, if necessary, the state's vendor file.

Person Responsible: Ron Lang, Director, Management Services Division
Rae Bly, Director, Appeals & Regulations

Estimated Completion Date: September 30, 1998

Audit Finding #8

DHS was not timely in its review of subrecipient audit reports.

Audit Recommendation #8

To ensure compliance with federal regulations and state policy, the department needs to review *the subrecipient reports in a more timely manner.*

Department Response #8

The department agrees with the recommendation.

Person Responsible: David Ehrhardt, Director, Internal Audits Office

Estimated Completion Date: July 31, 1998