



DEPARTMENT OF HUMAN SERVICES

861279

FINANCIAL AND COMPLIANCE AUDIT

FOR THE THREE YEARS ENDED JUNE 30, 1985

NOT FILMED

Financial Audit Division  
Office of the Legislative Auditor  
State of Minnesota

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**DEPARTMENT OF HUMAN SERVICES      881279**  
**FINANCIAL AND COMPLIANCE AUDIT**  
**FOR THE THREE YEARS ENDED JUNE 30, 1985**

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**AUGUST 1986**

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**Financial Audit Division**  
**Office of the Legislative Auditor**  
**State of Minnesota**



STATE OF MINNESOTA

OFFICE OF THE LEGISLATIVE AUDITOR

VETERANS SERVICE BUILDING, ST. PAUL, MN 55155 • 612/296-4708

JAMES R. NOBLES, LEGISLATIVE AUDITOR

Senator Randolph W. Peterson, Chairman  
Legislative Audit Commission

Members of the Legislative Audit Commission

Mr. Leonard W. Levine, Commissioner  
Department of Human Services

Audit Scope

We have completed a financial and compliance audit of the Department of Human Services Central Office for the three years ended June 30, 1985. Section I provides a brief description of the department's activities and finances. Our audit was made in accordance with generally accepted auditing standards, and the standards for financial and compliance audits contained in the U.S. General Accounting Office Standards for Audit of Governmental Organizations, Programs, Activities, and Functions, and accordingly, included such audit procedures as we considered necessary in the circumstances. Our audit procedures are further described in the audit techniques section of this letter. Field work was completed on May 30, 1986.

We have issued separate management letters, dated March 30, 1984, February 21, 1985, and February 18, 1986, as part of our Statewide Financial and Single Audit work in the department for fiscal years 1983, 1984, and 1985. The management letters contained 34 recommendations for fiscal year 1983, 37 recommendations for fiscal year 1984, and 11 recommendations for fiscal year 1985, relating primarily to the administration of state and federal programs by the department.

The audit objectives were to:

- study and evaluate major internal control systems at the Department of Human Services Central Office, including a review of receipts, payroll, fixed assets, administrative and grant disbursements;
- verify that financial transactions were made in accordance with applicable laws, regulations, and policies, including Minnesota Statutes Chapters 252 to 259, and other finance-related laws and regulations;
- verify that financial transactions were properly recorded in the Statewide Accounting (SWA) System; and
- determine the status of prior audit recommendations relating to Central Office financial management of the state regional centers and nursing homes.

The Department of Human Services manages eight regional human service centers and two nursing homes. These institutions are not a part of the scope of this audit. Separate institution audits are conducted by our office and individual reports are issued to the Commissioner of Human Services and the Chief Executive Officers.

#### Management Responsibilities

The management of Human Services is responsible for establishing and maintaining a system of internal accounting control. In fulfilling this responsibility, estimates and judgements by management are required to assess the expected benefits and related costs of control procedures. The objectives of a system are to provide management with reasonable, but not absolute assurance that assets are safeguarded against loss from unauthorized use or disposition, and that transactions are executed in accordance with management's authorization and recorded properly.

Because of inherent limitations in any system of internal accounting control, errors or irregularities may occur and not be detected. Also, projection of any evaluation of the system to future periods is subject to the risk that procedures may become inadequate because of changes in conditions, or that the degree of compliance with the procedures may deteriorate.

The management of Human Services is also responsible for the department's compliance with laws and regulations. In connection with our audit, we selected and tested transactions and records from the programs administered by the department. The purpose of our testing of transactions was to obtain reasonable assurance that Human Services had, in all material respects, administered its programs in compliance with applicable laws and regulations.

#### Audit Techniques

The Statewide Financial and Single Audit for the three years ended June 30, 1985, covered material state and federal programs such as Medical Assistance, Aid to Families With Dependent Children, Social Services, General Assistance, and Federal Administrative Aids. This departmental audit which also covered the three years ended June 30, 1985 supplements the Statewide Financial and Single Audit and was specifically designed to review Central Office administrative expenditures, including payroll, travel, contractual services, and other operating expenses. We also examined five of the largest state programs listed below which were not subject to review during the 1983-1985 Statewide Audits.

- Adult Mental Illness Residential Grants
- Mental Health - Chronic Mental Illness Grants
- Semi-Independent Living Services
- American Indian Chemical Dependency Grants
- Equalization Aid

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Mr. Leonard W. Levine, Commissioner  
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Conclusions

In our opinion, except for the issues addressed in Section II, recommendations 1-8, and except for the issues raised in our management letter dated February 18, 1986, recommendations 2, 4, 7, 8, 9, 10 and 11, the Department of Human Services Central Office system of internal accounting control in effect on March 31, 1986, taken as a whole, was sufficient to provide management with reasonable, but not absolute assurance, that assets are safeguarded against loss from unauthorized use or disposition, and that transactions are executed in accordance with management's authorization.

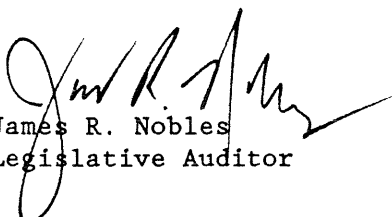
In our opinion, except for the issue discussed in Section II, recommendation 3, for the years ended June 30, 1983, 1984, and 1985, the financial transactions of the Department of Human Services Central Office were properly recorded in the statewide accounting system.

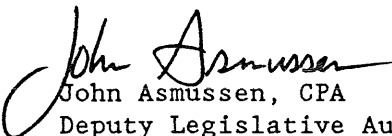
In our opinion, except for the issues raised in our management letters dated March 30, 1984, recommendations 9 and 17, February 21, 1985, recommendation 25, and February 18, 1986, recommendations 1, 3, 5, and 6, for the years ended June 30, 1983, 1984, and 1985, the Department of Human Services Central Office administered its programs in compliance, in all material respects, with Minn. Stat. Chapters 252 to 259, and applicable finance-related laws and regulations.

Section II of this Audit Report contains the recommendations we developed during this audit. It is presented to assist you in improving accounting procedures and controls. We will be monitoring and reviewing your progress on implementing these recommendations.

A summary of the progress made on the prior audit recommendations relating to the Central Office financial management of the state regional centers and nursing homes for the year ended June 30, 1984, dated September 13, 1985, is shown in Section III. This section is entitled "Status of Prior Audit Recommendations and Progress Toward Implementation." All prior audit recommendations related to the financial management of the state centers and homes were implemented, or substantially implemented, or withdrawn.

We would like to thank the Department of Human Services Central Office staff for the cooperation extended to us during this audit.

  
James R. Nobles  
Legislative Auditor

  
John Asmussen, CPA  
Deputy Legislative Auditor

August 7, 1986

DEPARTMENT OF HUMAN SERVICES  
CENTRAL OFFICE

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AUDIT PARTICIPATION

The following members of the Office of the Legislative Auditor participated in this audit:

|                        |                            |
|------------------------|----------------------------|
| John Asmussen, CPA     | Deputy Legislative Auditor |
| Renee Redmer           | Audit Manager              |
| Jack Hirschfeld, CPA   | Auditor-in-Charge          |
| Brad White             | Staff Auditor              |
| Beth Widstrom-Anderson | Staff Auditor              |
| Judy Holthusen         | Staff Auditor              |
| Becky Finley           | Intern                     |

EXIT CONFERENCE

The findings and recommendations in this report were discussed with the following staff of the Department of Human Services Central Office on June 16, 1986:

|                  |   |
|------------------|---|
| Leonard Levine   | Commissioner                              |
| Francis Giberson | Deputy Commissioner                       |
| Francis Moriarty | Assistant to the Commissioner             |
| Ken Gosset       | Assistant Commissioner                    |
| Jon Darling      | Director, Financial Management Division   |
| James Walker     | Director, Residential Facilities Division |

DEPARTMENT OF HUMAN SERVICES  
CENTRAL OFFICE

I. INTRODUCTION

The Department of Human Services (DHS), formerly the Department of Public Welfare, was established to develop and supervise a broad range of social service and public assistance programs.

Major activities of DHS include:

- operation of the state regional centers and nursing homes;
- providing community services for the aged, deaf and hearing impaired, and the blind and visually handicapped;
- providing medical care, social services, and financial assistance needed by poor, aged, abused, vulnerable and disadvantaged citizens; and
- supervising the legal and administrative framework in which county administrative and service organizations operate.

Activities of DHS are financed primarily through General Fund appropriations and federal grants. Fiscal year 1985 Central Office expenditures, including encumbrances, on a budgetary basis, were as follows:

|                                      | <u>GENERAL<br/>FUND</u>  | <u>FEDERAL<br/>FUND</u>  | <u>OTHER<br/>FUNDS</u>  | <u>TOTAL</u>               |
|--------------------------------------|--------------------------|--------------------------|-------------------------|----------------------------|
| Grants and Aids                      | \$800,455,182            | \$803,501,463            | \$15,915,381            | \$1,619,872,026            |
| Personal Services                    | 19,200,828               | 4,543,220                | 25,896                  | 23,769,944                 |
| Contractual Services                 | 2,379,714                | 175,484                  | 101,747                 | 2,656,945                  |
| Travel & Subsistence                 | 675,673                  | 253,825                  | 6,761                   | 936,259                    |
| Supplies & Equipment                 | 1,133,464                | 864,173                  | 156,083                 | 2,153,720                  |
| Redistributed Costs                  | 3,191,654                | 14,944,554               | 7,429,066               | 25,565,274                 |
| Other Administrative<br>Expenditures | <u>8,842,751</u>         | <u>2,780,541</u>         | <u>139,650</u>          | <u>11,762,942</u>          |
| <br>TOTAL                            | <br><u>\$835,879,266</u> | <br><u>\$827,063,260</u> | <br><u>\$23,774,584</u> | <br><u>\$1,686,717,110</u> |

The Commissioner, Leonard Levine, is the administrative head of the department.

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II. CURRENT FINDINGS AND RECOMMENDATIONS

The Department of Human Services does not expediently process all contracts and evaluations nor properly record certain contracted services in the statewide accounting system.

The Department of Human Services (DHS) Central Office expended approximately \$15 million for professional and technical services in fiscal year 1985. We reviewed 148 contracts for various state and federal programs during the years ended June 30, 1983, 1984 and 1985. The following areas of noncompliance with state administrative policies governing contracted services were identified:

1. Contractual services were rendered and liabilities were incurred by Central Office before the written agreements were finalized.

Minn. Stat. Section 16A.15, Subd. 3 requires that funds be encumbered prior to any obligation. Subd. 3 also provides that, "a claim presented against an appropriation without prior encumbrance may be made valid on investigation, review and approval by the Commissioner of Finance, if the services, materials, or supplies to be paid for were actually furnished in good faith without collusion and without intent to defraud."

Finance procedures require state agencies to submit letters of explanation for incurring contractual service and other obligations prior to the encumbrance of funds. These letters must be authorized by Finance prior to the payment of consultant services, otherwise employees may be held liable for incurring these obligations. Finance Operating Procedure 06:04:05 provides that contracts are to be signed prior to their effective date. The DHS Policy and Procedure Manual also states that, "under no conditions should an agency permit a contractor to start work thereby creating an obligation on the part of the state, until the contract has been fully executed and copies are in the possession of both the agency and the contractor."

Our review disclosed that 145 (\$9,228,143) of the 148 (\$9,276,252) contracts examined, or 98 percent, were signed and encumbered after the contractual services had begun. For each of the three fiscal years examined, both the Chemical Dependency and Refugee Assistance Program staff did not finalize their contracts until several weeks after the service period had begun. The following chart shows the program name, number and amount of contracts processed late. The range of time between the date of obligation (beginning date of contractual services) and the date of final encumbrance (signatures finalized on contracts) are also shown for the respective number of contracts.



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SCHEDULE OF CONTRACT DELAYS  
YEARS ENDED JUNE 30, 1983, 1984, AND 1985

| <u>Program</u>                       | <u>Number of<br/>Contracts</u> | <u>Amount</u>      | <u>Contract<br/>Delays</u> |
|--------------------------------------|--------------------------------|--------------------|----------------------------|
| Chemical Dependency                  | 106                            | \$6,980,955        | 2-4 months                 |
| Refugee Assistance                   | 29                             | 1,514,679          | 1-3 months                 |
| Health Care Professional Services    | 5                              | 109,240            | 1-2 months                 |
| Mentally Retarded                    | 1                              | 55,000             | 12 months                  |
| Nursing Home Bill Management Studies | 1                              | 447,000            | 3 months                   |
| Compulsive Gambler Treatment         | 1                              | 15,400             | 1 month                    |
| Child Welfare Family Social Services | 1                              | 76,969             | 1 month                    |
| Family Child and Adult               | <u>1</u>                       | <u>28,900</u>      | 2 months                   |
| TOTAL                                | <u>145</u>                     | <u>\$9,228,143</u> |                            |

DHS program staff sent Minn. Stat. Section 16A.15, Subd. 3 letters of explanation to the Department of Finance for many of the late contracts. We located 111 letters in the department that had been submitted to Finance for authorization prior to payment. For the remaining 34 contracts, we were unable to locate letters of approval in the department. Although DHS program staff submitted many letters of explanation to Finance for approval, we are concerned that DHS program staff consistently enter into contractual service agreements before the documents are signed and the encumbrances are established. If the contracts are not approved, the department would incur unauthorized obligations for the state or federal government. Failure to comply with state contract policies increases the risk that DHS employees may be held liable for incurring unauthorized liabilities.

Department staff offered a variety of reasons for the delays in processing contracts. However, since most of the contracts that we reviewed were for routine and recurring program services, we believe that DHS staff should have had sufficient lead time to complete the annual internal and external contract review process.

Finance Procedure 06:04:05 provides that any change to an existing contract which involves increased cost to the agency must be requisitioned before the contractor signs the amendment. Two contracts totaling \$109,337, one for Health Care Professional Services and the other for Child Welfare Family Social Services, were amended and signed by the contractor before funds were requisitioned. One of the amendments was signed 28 days before the funds were requisitioned. Again, obligations should not be incurred prior to the date funds are encumbered.

DHS program staff should plan their contractual agreement process more timely to ensure that contracts, amendments and encumbrance documents are finalized before the services begin. The 16A.15 provision for letters of explanation should be used only in emergency situations and should not become a common operating practice of the department.

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2. Evaluations of contractors' performance were not completed timely.

The Department of Administration - Policy and Procedure Statement 188, provides that an evaluation of contractor performance should be completed within 30 days of the completion of the contract. The evaluations are used by Administration to ensure that the services performed under state contracts are satisfactory. The evaluations are also used to select future contractors.

We reviewed 13 contracts for fiscal year 1985 to determine if the evaluations were completed timely. As of March 24, 1986, evaluations had not been filed for eight contracts totaling \$282,609 for the following programs:

| <u>Program</u>                           | <u>Number of Contracts</u> |
|--|----------------------------|
| Health Care Professional Services        | 4                          |
| Management Operations - Special Services | 1                          |
| Compulsive Gambler Treatment             | 1                          |
| Child Welfare Family Social Services     | 2                          |

All of these contracts were completed prior to July 1, 1985. Central office should file timely evaluations of contractors' performance with the Department of Administration to ensure proper completion of the evaluation process.

3. Contracted services were not properly recorded in the Statewide Accounting System.

Professional and technical services are to be classified as object code of expenditure 15x or 16x in the Statewide Accounting (SWA) System. However, professional services totaling approximately \$12 million were coded 742 and 792, grants and aids, in the SWA system during fiscal year 1985 for the Chemical Dependency and Refugee Assistance Programs. Central Office program staff agree that these agreements for professional services are contractual services and not grants. Many of the contractual service administrative procedures promulgated by the Departments of Finance and Administration are followed by Central Office. For example, competitive negotiation procedures are used for both the Chemical Dependency and Refugee Assistance Programs. Therefore, we believe that these agreements should be classified as object codes 15x or 16x.

RECOMMENDATIONS:

1. DHS should establish internal operating procedures to ensure that contractual service agreements and amendments are finalized prior to date that the services begin. Minn. Stat. Section 16A.15, Subd. 3 letters of explanation should only be used in emergency situations.

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2. *DHS should ensure that evaluations of contractors' performance are completed within 30 days after the contract completion date.*
3. *DHS should code professional and technical services for the Chemical Dependency and Refugee Assistance Programs to either 15x or 16x in the SWA system.*

The DHS Audits and Appeals Division has not completed the required number of on site audits of the nursing homes as specified in the Minnesota Statutes.

Minn. Stat. Section 256B.30 provides that every licensed health care facility shall submit an annual financial audit to the Commissioner of Human Services. Public accounting firms conduct the annual financial audits of the nursing homes. Minn. Stat. Section 256B.27, Subd 2A also requires the Commissioner to provide on site audits of the cost reports of nursing homes participating as vendors of the Medical Assistance Program. The statute further states that the Commissioner shall select for audit five percent of the nursing homes at random, and another 20 percent based on factors such as changes in ownership, complaints, or other reported problems. This statute requires that a total of 25 percent of the 460 nursing homes, amounting to approximately 115 homes, be audited on an annual basis. Historically, the DHS Audits and Appeals Division has been assigned the responsibility to perform the on site audits of the cost reports for the nursing homes. However, the division only completed 59 audits in fiscal year 1983, 30 in fiscal year 1984, and 18 audits in fiscal year 1985.

Discussions with the Audits and Appeals Division staff indicated that responsibility for other functions such as establishing rates for the 460 nursing homes and 300 residential facilities for the mentally retarded, and processing rate appeals has reduced the amount of time available to do on site audits of the nursing homes. The division currently employs approximately 30 staff to administer their responsibilities. The department estimates that a savings of \$1.37 million (Medical Assistance Payments-State Share) would be achieved by an additional 12 field auditors conducting on site nursing home audits.

In an attempt to obtain more staff to complete the required audits, the department requested a \$400,000 appropriation during the 1986 legislative session. The appropriation was not approved; however, the Governor directed the department to use savings in non-salary accounts for additional staffing. On April 11, 1986 the department requested the approval of the Legislative Advisory Commission (LAC) to transfer non-salary monies to the field audit special projects salary account. On May 29, 1986, the LAC authorized \$335,400 for 12 auditor positions during the period June 1, 1986 to June 30, 1987. However, these positions are non-complement and unclassified and will only be utilized for the duration of this period.

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Controls over the accuracy of the nursing home cost reports will be decreased and the Medical Assistance savings projected by the department may not be achieved if a sufficient number of nursing home audits are not completed. If staffing for future years is insufficient, the department could consider other alternatives such as amending Minn. Stat. Section 256B.27, Subd. 2A to allow the division more flexibility in determining the number and frequency of audits required. The department could also consider coordinating their efforts with the firms conducting the financial audits to increase coverage of significant compliance issues. Audit procedures could be developed for the firms to incorporate compliance tests of the cost reports into the financial audits. Again, statutory revision to Minn. Stat. Section 256B.30 could be considered to include compliance issues in the annual audit requirements for the nursing homes.

*RECOMMENDATION:*

4. *DHS should review the various alternatives to ensure compliance with the statutory audit requirements. DHS should also consider amending the statutes to allow more flexibility in determining the number and frequency of audits and to increase reliance upon the audits conducted by public accounting firms.*

DHS did not equitably reimburse nor distribute all available funds to the counties participating in the Semi-Independent Living Services Program.

The Semi-Independent Living Services Program (SILS) provides state grants to counties to train mentally retarded persons for independent living or for staying in a semi-independent living arrangement. DHS did not equitably allocate the 1985 appropriation to the counties and returned unallocated moneys to the General Fund. Minn. Stat. Section 252.275 provides the following:

- Subd. 2. Application; criteria. To apply for a grant, a county board shall submit an application and budget to the Commissioner of Human Services. The Commissioner shall make grants only to counties whose applications and budgets are approved.
- Subd. 3. Reimbursement. On or before September 1 of each year, the Commissioner shall allocate available funds to the counties which have approved plans and budgets. The Commissioner shall disburse the funds on a quarterly basis during the fiscal year to reimburse counties for costs incurred in providing services to individual clients in accordance with the approved plans and budgets.
- Subd. 4. Formula. The Commissioner shall allocate grants under this section to finance up to 95 percent, but not less than 80 percent, of each county's cost for semi-independent living services for mentally retarded persons.



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Subd. 6. Rules. The Commissioner shall adopt rules to govern grant applications, criteria for approval of applications and allocation of grants.

Minnesota Rules further describe the grant and reimbursement processes. Minn. Rules Part 9525.0960, subp. 2 provides that counties shall submit annual proposals and projected service costs for approval of a grant award by the Commissioner of Human Services. Minn. Rules Part 9525.0970, subp. 1 states that county boards shall be paid by the state agency based on their actual expenditures to eligible clients and the rate of reimbursement determined by the Commissioner based on the county's proposal. The amount of state reimbursement to a county must not exceed the amount of the state grant made to the county board for the grant period. Minn. Rules Part 9525.0970, subp. 2 further provides that the actual percentage of the total costs of semi-independent living services paid by the Commissioner shall be the percentage of total expenditures for services budgeted by county boards and approved by the Commissioner for reimbursement for the grant period prorated against the state appropriation for the period. The Commissioner shall work with the county board to adjust proposals as necessary to comply with Minn. Stat. Section 252.275, Subd. 4. Priority funding shall also be given to eligible clients who have received services in the previous grant period and continue to need services during the proposal grant period. Minn. Rules Part 9525.0990 authorizes the Commissioner to increase a grant award to a county when:

- it has been determined that unused grant money is available;
- the grant increase is within the limits established by the statutes; and
- the county expenditures exceeded their budget projections.

Payments shall be in the form of an initial advance, with subsequent quarterly payments contingent upon receipt of a completed financial report from the county board. If actual expenditures are less than provided in its approved budget, the Commissioner shall reduce the quarterly payments so that the grant remains within the limits in Minn. Rules Part 9525.0970.

During the 1983-1985 biennial budget process, DHS requested and was appropriated \$2,674,300 by the Legislature for fiscal year 1985 SILS program reimbursements. Total actual expenditures incurred by the counties for 1985 were \$3,570,750, or \$896,450 more than the amount appropriated. The appropriation was \$182,300 less than the \$2,856,000 needed to fund the counties 80 percent of their 1985 costs. DHS reimbursed the counties \$2,573,864 which in total approximates 72 percent of the total counties' expenditures. An unexpended appropriation balance of \$100,436 (\$2,674,300 - \$2,573,864) which could have been reimbursed to the counties was returned by DHS to the General Fund.

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Due to the complex and conflicting program regulations and cumbersome departmental distribution process, the final yearly reimbursements to the counties were also inequitable. Thirty counties received 80 percent of their actual yearly expenditures and forty-four counties received less than 80 percent of their expenditures. One county received less than 35 percent of their actual costs.

Grant awards were originally calculated by DHS based on the appropriation of \$2,674,300. Eighty percent of the counties annual budgeted amounts for existing clients was allocated and the remainder of the appropriation was prorated among new clients (47 percent). Grant award letters were sent to the counties notifying them of this allocation by September 1, 1984. However, the counties were not reimbursed for the original allocation for the year. Instead, grant awards were periodically adjusted during the year based on revised expenditure data and actual number of new and existing clients enrolled in the program. The DHS allocation and distribution method was as follows:

- Each county was advanced 20 percent of the original allocation in September 1984.
- In the second quarter, counties were reimbursed 80 percent of their actual costs reported for the first quarter.
- Counties were reimbursed a portion, arbitrarily determined by DHS, of their actual costs for the second quarter.
- Grant awards were adjusted after the second quarter based on the counties actual expenditures incurred for the first half of the year and discussions with the county administrators.
- Counties were reimbursed a portion of their actual costs for the third quarter. Some grant awards were further adjusted based on new data.
- Upon receipt of the counties' final expenditure reports for 1985, final distributions were made as follows:
  - 80 percent of the final yearly reported expenditures were reimbursed up to the last adjusted grant award amount; and
  - no differentiation was made on the reimbursement rate for new or existing clients, 80 percent was applied for all clients.

We believe that this method of distributing SILS program funds resulted in an inequitable allocation. Counties that underestimated annual expenditures received less than counties that overestimated expenditures. Counties that incurred more expenditures in the first half of the year also received more than counties that expended less, although these counties may have expended more later in the year for new clients.

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DHS should consult with the Office of the Attorney General to determine what legal remedies are available, if any, to adjust the 1985 distribution of SILS program funds. The department should also review the statutory requirements and process for calculating and distributing future SILS funds to ensure an equitable allocation system.

The department should consider amending the regulations to ensure clarity of the distribution process. The conflicting legal provisions such as the 80 percent minimum reimbursement requirement and proration authority should be clarified in the statutes and rules. The department should also review the appropriation process to determine if the amounts requested should be increased or if alternate funding mechanisms should be established.

*RECOMMENDATIONS:*

5. *DHS should work with the Office of the Attorney General to determine the appropriate legal basis for distributing SILS funds.*
6. *DHS should review the distribution and appropriation process to determine an appropriate and equitable funding mechanism.*

DHS did not prepare certain reports as required by a grant agreement with the McKnight Foundation and did not review the proper application of certain expenditures to the grant funds.

The McKnight Foundation has provided DHS \$1,422,383 in grants for the three years ended June 30, 1985. These grants were given to DHS to fund community based projects for the aging (\$1,050,000), to help fund the health interpreter needs of refugees (\$226,383), and to augment federal funds for mental health services for American Indians (\$146,000).

A written agreement was developed for each grant between the foundation and DHS stipulating the purpose of the grant, the payment terms, and the financial and evaluation reporting requirements. For example, the grant agreement related to the mental health services for American Indians provided:

- the purpose and amount of the grant;
- payment terms and dates;
- financial requirements, including the requirement of a report comparing budgeted and actual costs with remaining line item balances; and
- reporting requirements, including the requirement of quarterly progress reports and a final program report.

DHS did not prepare the financial reports for budgeted and actual costs for the mental health services for American Indians grant. They also did not prepare the final program reports for the American Indians grant due August 1985, and for the refugee assistance grant due October 1983.

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We also found that an expenditure of \$2,600 for 1985 relating to the community-based projects for the aging was incorrectly charged to a federal account, Special Programs for the Aging. A balance of approximately \$27,000 was shown in the community-based projects account at June 30, 1986. A correction should be made to credit the federal account and properly charge this expenditure to the community-based projects account. The department should periodically review grant expenditures to ensure that the proper source of funds are used.

*RECOMMENDATION:*

7. *DHS should:*

- *comply with the reporting requirements of the grant agreements with nonprofit organizations; and*
- *transfer \$2,600 to the Special Program for the Aging - Federal account.*

Initial payments for equalization aid to counties are not being made in accordance with statutory deadlines.

Equalization aid totaling \$1.4 million in fiscal year 1985 was provided to counties with the lowest taxing capability and highest welfare costs relative to other counties. Minn. Stat. Section 245.74, Subd. 3 requires that initial payments for equalization aid to counties be made on or before October 1 and final payments be made by January 1 of the following fiscal year. The equalization aid to counties is determined by a formula that includes four factors:

- Recipient Rate: This is the average number of income maintenance requests per month per 10,000 people, and is based on estimates from the state demographer's office. This information was received annually in September.
- Per Capita Income: The U.S. Census Bureau provides this information to DHS in November of every other year.
- Per Capita Taxable Value: These figures are determined by the Department of Revenue in July of each year and represents the total assessed value.
- Per Capita Expenditures for Welfare: The amount of the net welfare costs is compiled in December by DHS Financial Management Division.

DHS did not comply with the statutory deadlines for the initial payments during fiscal years 1983, 1984 and 1985. For fiscal years 1983 and 1984 initial payments were six months late, and the 1985 payment was over four months late. However, the final payments were completed before the statutory deadlines.



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The current formula which provides the entitlement for each county is dependent upon a ranking incorporating all four factors; therefore, all data is needed before the initial payments can be calculated. However, department staff indicated that certain of the required data elements cannot be obtained timely to finalize the entitlement calculations and to make the initial payments by October 1. The U.S. Census Bureau per capita income information is received after November biennially. The per capita expenditures for welfare are not compiled by DHS until December each year. The department currently cannot estimate the initial payments annually, since the formula results in entitlements to counties that fluctuate dramatically between years. For instance, one county's entitlement amounted to \$360,000 in fiscal year 1983, but only \$58,000 in fiscal year 1984. DHS is currently in the process of revising the distribution formula to prevent fluctuating entitlements to counties between fiscal years allowing them to make estimated initial payments.

*RECOMMENDATION:*

8. *The department should revise the calculation process or amend the statutory payment date.*

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III. STATUS OF PRIOR AUDIT RECOMMENDATIONS  
AND

PROGRESS TOWARD IMPLEMENTATION

CENTRAL OFFICE FINANCIAL MANAGEMENT OF  
THE REGIONAL CENTERS AND NURSING HOMES

Improved coordination and review of the financial policies and procedures for the state hospitals and nursing homes is needed.

1. Central Office should increase its role in coordinating and monitoring the financial activities and procedures of the various state hospitals and nursing homes, in part, through:
  - updating the Institutions Manual or other appropriate document to provide guidance to the institutions on the proper procedures for fiscal operations; and
  - establishing a monitoring function to periodically review the operations of the institutions to ensure compliance with established policies.

*RECOMMENDATION SUBSTANTIALLY IMPLEMENTED. A committee was formed by the Residential Facilities Division on July 1, 1985, to update the Institutions Manual. Over 25 procedures were developed during fiscal year 1986. Although many of these procedures related to program issues rather than fiscal management, we believe the department has instituted a process to establish fiscal and program guidance for the institutions.*

*The Residential Facilities Division has established a monitoring function to review fiscal problem areas and to provide guidance to the institutions when necessary.*

2. Residential Facilities should assist the institutions in developing procedures to provide administrative direction for the business aspects of the pre-vocational training and resident work programs.

*RECOMMENDATION SUBSTANTIALLY IMPLEMENTED. The Residential Facilities Division held meetings in 1986 with institution staff on the business aspects of the pre-vocational training and resident work programs. Our most recent audits of Brainerd, Fergus Falls, and Faribault indicated that these institutions developed internal written procedures to implement many of our prior audit recommendations relating to vocational programs.*

DEPARTMENT OF HUMAN SERVICES  
CENTRAL OFFICE

3. Central Office should seek amendment to the statutes for clarification of the wage requirements applicable to the resident training and work programs.

*RECOMMENDATION SUBSTANTIALLY IMPLEMENTED.* The department introduced a bill during the 1986 legislative session to clarify the applicability of Minn. Stat. Section 246.151. The bill passed the Senate but the House adjourned prior to taking any action on the file. DHS should reintroduce the bill in the next legislative session. Our audits of the Brainerd, Fergus Falls, and Faribault resident training and work programs indicated that certificates of exemption from the federal minimum wage requirements had been obtained from the U.S. Department of Labor. Therefore, we believe the department is in substantial compliance with state and federal minimum wage laws.

4. Residential Facilities, with the assistance of the Department of Education, should work with the institution staff to ensure an adequate understanding of the Child Nutrition Program guidelines. Specifically, Central Office should ensure that institution staff understand that:

- information included on the institutions monthly payment vouchers and financial reports should be determined in accordance with program guidelines; and
- the institutions should request the maximum reimbursement they are entitled to receive from the program.

*Recommendation Implemented.* In addition to the procedures developed by the institutions, the Department of Education provided written guidelines for including the proper information on payment vouchers and financial reports. As a result, the institutions started requesting the maximum reimbursement they were entitled to receive from the Child Nutrition Program in fiscal year 1984.

5. Central Office should develop written agreements between the department, the appropriate institutions and the Services for the Blind for canteen operations.

*RECOMMENDATION WITHDRAWN.* Since the Services for the Blind is currently under the jurisdiction of the Department of Jobs and Training, DHS should pursue this area with Jobs and Training.



STATE OF MINNESOTA  
DEPARTMENT OF HUMAN SERVICES  
CENTENNIAL OFFICE BUILDING  
ST. PAUL, MINNESOTA 55155

August 7, 1986

Mr. James R. Nobles  
Legislature Auditor  
1st Floor Veterans Service Bldg.  
20 W. 12th Street  
St. Paul, MN 55155

Dear Mr. Nobles:

Attached are the Department of Human Services responses to the recommendations contained in the draft audit report for the financial and compliance audit for the three years ended June 30, 1985.

We understand that the responses will be printed with the final audit report.

Sincerely,

A handwritten signature in cursive script, appearing to read "Leonard W. Levine".

LEONARD W. LEVINE  
Commissioner

cc: Frank Giberson  
Renee Redmer  
Jon Darling



DEPARTMENT OF HUMAN SERVICES  
RESPONSES TO FINANCIAL AND COMPLIANCE AUDIT  
THREE YEARS ENDING JUNE 30, 1985

RESPONSE TO RECOMMENDATION #1:

The Department of Human Services is in the process of revising the DHS Contracting Procedures Manual. As part of the manual revision process, suggested "timelines" for contract development are being developed to ensure that sufficient time is allowed for contracts to be finalized prior to the date that the contracted services begin. Gerald Joyce (Financial Management Division) and Rae Bly (Appeals and Regulations Division) are responsible for the revision of the Contracts Manual. The projected date for completion is November 21, 1986.

In addition to revising the Contracts Manual and developing timelines, the Department is also planning a contracts training course for Department personnel who are involved in developing contracts for the Department. The training course is being planned by Rae Bly, and will be held on November 21, 1986. The course will include a review of contracting procedures and the distribution and discussion of the new manual material.

RESPONSE TO RECOMMENDATION #2:

The current DHS Contracting Procedures Manual specifies that an evaluation of a contractors' performance must be completed within 30 days of the completion of the contract. The responsibility for completing the evaluation, as well as the responsibility for diligent administration and monitoring of the contract, rests with the Department personnel who originate the contract. This information will be highlighted in the revised manual material and discussed in the training course.

RESPONSE TO RECOMMENDATION #3:

The area of proper expenditure classification for contracts and grant is ambiguous at best. The Department of Human Services feels that we have properly classified our contracts and grants. We would like to point out that all of our contracts and grants are approved through the Department of Administration Contracts Management section and through the Department of Finance. DHS has followed the Department of Administration rule in classifying contracts and grants. The rule is as follows: If a contractor is providing a service to the state then the proper classification is 15x or 16x; if the state is funding an outside entity to provide services to persons not employed by the state, then the proper classification is as a grant (7xx).

However, as mentioned above the area is ambiguous, so in response to this recommendation DHS will discuss the situation with the Departments of Administration and Finance and attempt to get clear and specific guidelines on expenditure classification which will be included in the contracts manual.

Person responsible: Jerry Joyce  
Projected completion date: November 1, 1986

RESPONSE TO RECOMMENDATION #4:

We agree that the required amount of on-site audits were not completed as specified in the Minnesota statutes. However, we do not agree with the recommendation as follows:

1. The answer to insure accuracy of the cost reports is to increase our on-site audits rather than postpone the audits or forgive the facility by not auditing. The Audit Division must become current in its field audit assignments so that the on-site audit is completed within 18 months of when the payment rate was established. This prompt action on our part would encourage the facilities to accurately report only their allowable costs. The only practical way of becoming current is the hiring of staff. We are currently attempting to convince the Legislature that an increase in staff is imperative. Both the Governor and Legislature agreed that an increase is necessary but only funded a one year project of 12 auditors. We are confident that the project will demonstrate the viability of the staff increase.
2. We do not believe that the Department can rely on the audits performed by public accounting firms (CPA). The Federal government reviewed a number of single audit reports submitted by CPA firms and found them to be very unsatisfactory for compliance issues (GAO/AFMD-86-20). Additionally, the CPA firms that produce the audited statements also prepare or review the facility's cost report. We feel that this would be too much of a potential conflict of interest to ignore.

Person responsible: Richard Archer  
Projected completion date: June 30, 1987

RESPONSE TO RECOMMENDATION #5 and #6:

After consulting with the Attorney General's Office, it is clear that Minnesota Statutes 252.275 allow the Commissioner to reimburse counties at various rates (from 80-95%) based on county's approved plans and budgets. Minnesota Statutes 252.275 and rules promulgated thereunder

provide an appropriate legal basis for allocating funds according to the Attorney General's Office. The Minnesota Rules in effect in Fiscal Year 1985 governing the administration of the SILS program were 12 MCAR S 2.02001-2.02011 [Temporary] and not Minnesota Rules, parts 9525.0900 to 9525.1020. Clearly, the variation of county reimbursement levels is not illegal or inequitable based on approved plans and budgets. Moreover, grants are based on county plans as approved by the Commissioner and the Commissioner is not authorized to exceed grant amounts. Counties can choose and have chosen to spend more than the Commissioner has approved for reimbursement. Since the 1985 allocation was neither illegal nor inconsistent with statute and rules, no legal remedy is needed.

Maintaining the minimum level of reimbursement for SILS has been and continues to be an emerging problem. The Department has requested funding from the legislature to assure that the minimum level is met, however, those funds were not granted. In 1985, even if the entire appropriation were allocated to counties, this minimum would not have been achieved.

The Department of Human Services will begin an immediate review of the following actions regarding the allocation of SILS with a view toward improving the administration of the program.

- Action 1     Seek legislative appropriation to assure eighty percent reimbursement is achieved. This would require about \$250,000 plus inflation each year of the next biennium.
- Action 2     Amend rules to add a settle-up period to assure that all available funds are distributed to counties and the Commissioner is authorized to adjust grants after the fiscal year ends.
- Action 3     Examine other allocation methods which are less administratively cumbersome, while allowing the Commissioner to target funding to achieve priorities established in Rule and Law.

A meeting has been scheduled with Legislative Audit staff to review in detail the findings and recommendations regarding the SILS program.

Person responsible: Robert F. Meyer  
Projected completion date: June 30, 1987

RESPONSE TO RECOMMENDATION #7:

Regarding the McKnight Indian Mental Health grant, we take exception to the finding that the Department did not meet the interim financial reporting requirement as stated in the award agreement. Detailed quarterly and year end reports were regularly submitted that included information on program and financial management activities. These reports described both the past activities as well as plans for the upcoming period. We assume the Foundation found these reports satisfactory (over a two year period), for they approved the \$43,000 supplemental grant in 1984 and the Department received no indication from the Foundation that our reports were not satisfactory.

We agree with the finding that a final report was not prepared. This document is being prepared and will be submitted by August 8, 1986. The person responsible is Alan Mathiason.

A final report on the Refugee Assistance grant was submitted to the Foundation. A copy will be supplied to Legislative Audit staff.

The incorrect payment of \$2,605.00 for a McKnight project from the federal 3-B program funds was corrected on April 1, 1986, at which time the Board on Aging accountant responsible for corrective action notified the legislative auditor performing the audit of the error and the correction of the same.

RESPONSE TO RECOMMENDATION #8:

Every effort will be made by the Department to make the initial Equalization Aid payments by the statutory date. It is expected that this effort will be successful and there will be no need to seek amendment of the initial payment date.

Person responsible: John Sellen  
Projected completion date: October 1, 1986



# NOTICE

State of Minnesota  
Office of the Legislative Auditor  
Veterans Service Building • St. Paul, MN 55155  
612/296-4708

## DEPARTMENT OF HUMAN SERVICES CENTRAL OFFICE

### Report Summary August 1986

The Office of the Legislative Auditor has released an audit report on the Department of Human Services (DHS) Central Office for the three years ended June 30, 1985. The report contains eight recommendations for improved procedures and controls.

The first three recommendations relate to the department's procedures for professional and technical service contracts. We recommended that DHS should establish internal operating procedures to ensure that contractual service agreements and amendments are finalized prior to the date that services begin. DHS should ensure that evaluations of contractors' performances are completed within 30 days after the contract completion date. DHS should also code professional and technical services properly in the Statewide Accounting System.

The fourth recommendation discussed compliance with the state statutory requirements for on site audits of the nursing homes. We recommended that DHS review the various alternatives to ensure compliance with the statutory audit requirements. DHS should also consider amending the statutes to allow more flexibility in determining the number and frequency of audits and to increase reliance upon the audits conducted by public accounting firms.

The fifth and sixth recommendations relate to the allocation of state aid for the Semi-Independent Living Services Program (SILS). DHS did not equitably reimburse nor distribute all available funds to the counties participating in the SILS Program in fiscal year 1985. We recommended that DHS should work with the Office of the Attorney General to determine the appropriate legal basis for distributing SILS funds. DHS should also review the distribution and appropriation process to determine an appropriate and equitable funding mechanism.

The seventh recommendation relates to the administration of McKnight Foundation grants. DHS did not prepare certain reports as required by the grant agreement with the foundation and did not review the proper application of certain expenditures to the grant funds. We recommended that DHS comply with the reporting requirements and transfer \$2,600 to the Special Program for the Aging-Federal Account.

Finally, initial payments for equalization aid to counties are not being made by DHS in accordance with state statutory deadlines. We recommended that the department review the calculation process or amend the statutory payment date.

The report includes the status of prior audit recommendations relating to DHS financial management of the state regional centers and nursing homes. All five recommendations were implemented, substantially implemented, or withdrawn.

The DHS response to the current recommendations is included within the report.



Office of the Legislative Auditor  
Veterans Service Building, Saint Paul, Minnesota 55155