

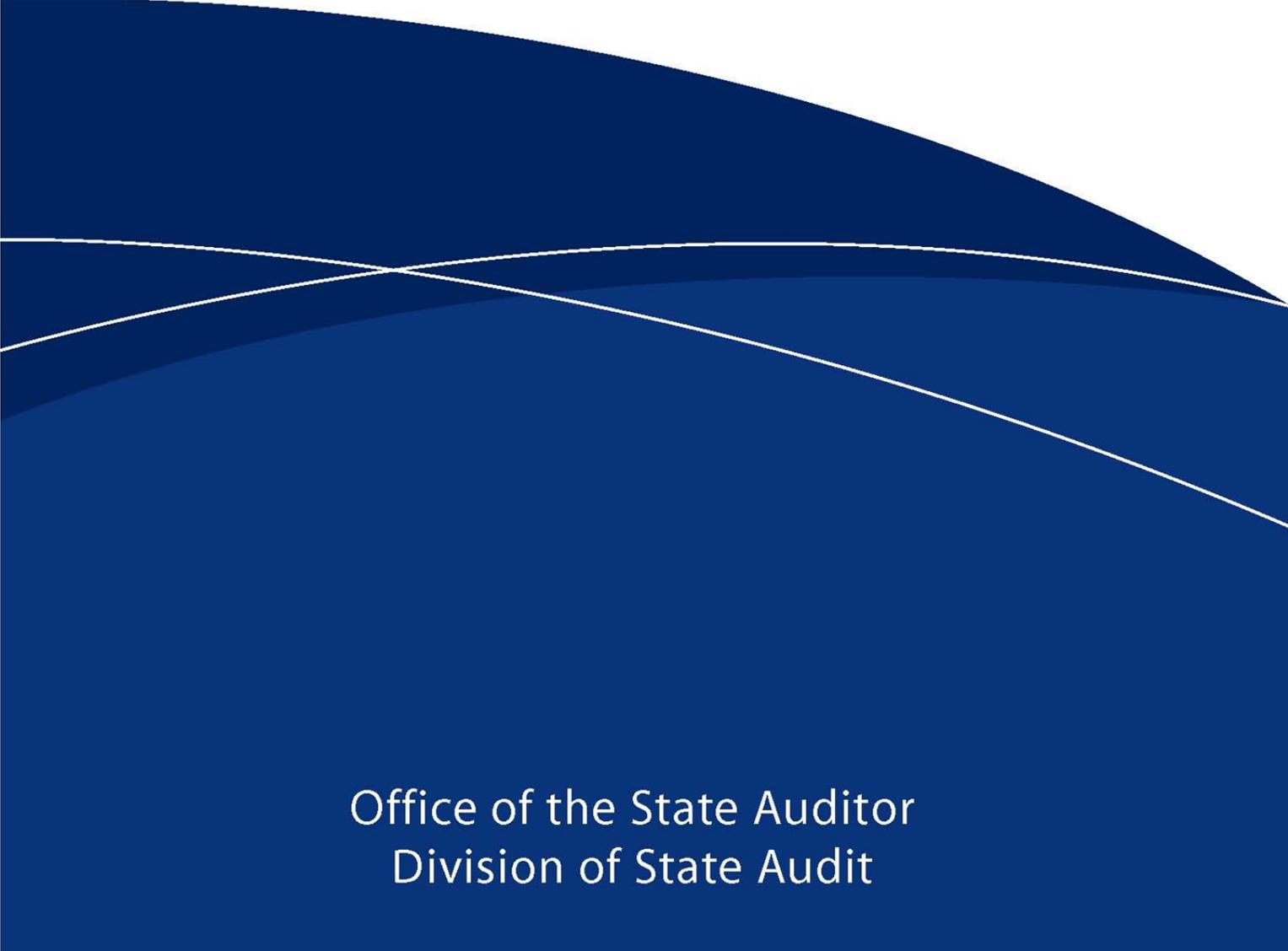
Department of Human Services

BISMARCK, NORTH DAKOTA

Audit Report

For the Biennium Ended
June 30, 2011

ROBERT R. PETERSON
STATE AUDITOR



Office of the State Auditor
Division of State Audit

**LEGISLATIVE AUDIT AND FISCAL REVIEW
COMMITTEE MEMBERS**

Representative Dan Ruby – Chairman
Senator Terry M. Wanzek – Vice Chairman

Representatives

Dick Anderson
Tracy Boe
Patrick Hatlestad
RaeAnn G. Kelsch
Keith Kempenich
Gary Kreidt
Joe Kroeber
Andrew Maragos
Corey Mock
David Monson
Chet Pollert
Bob Skarphol
Lonny Winrich
Dwight Wrangham

Senators

Randel Christmann
Joan Heckaman
Jerry Klein
Judy Lee

Contents

<i>Transmittal Letter</i>	<i>1</i>
<i>Executive Summary</i>	<i>2</i>
<i>Introduction</i>	<i>2</i>
<i>Responses to LAFRC Audit Questions</i>	<i>2</i>
<i>LAFRC Audit Communications</i>	<i>3</i>
<i>Audit Objectives, Scope, and Methodology</i>	<i>5</i>
<i>Discussion and Analysis</i>	<i>7</i>
<i>Financial Summary</i>	<i>7</i>
<i>Analysis of Significant Variances - Budgeted and Actual Expenditures</i>	<i>8</i>
<i>Financial Statements</i>	<i>9</i>
<i>Statement of Revenues and Expenditures</i>	<i>9</i>
<i>Statement of Appropriations</i>	<i>10</i>
<i>Internal Control</i>	<i>14</i>
<i>Control/Fraud Risk Assessment Activities (Finding 11-1)</i>	<i>15</i>
<i>Inadequate Controls Surrounding Revenue Collections (Finding 11-2)</i>	<i>15</i>
<i>Provider Enrollment Controls Weakness (Finding 11-3)</i>	<i>17</i>
<i>Lack of Internal Controls at State Hospital's Commissary (Finding 11-4)</i>	<i>18</i>
<i>Financial Reporting Errors (Finding 11-5)</i>	<i>19</i>
<i>Lack of Child Care Assistance Controls (Finding 11-6)</i>	<i>20</i>
<i>Compliance With Legislative Intent</i>	<i>22</i>
<i>Operations</i>	<i>25</i>
<i>Prior Recommendations Not Implemented</i>	<i>26</i>
<i>Management Letter (Informal Recommendations)</i>	<i>27</i>



STATE OF NORTH DAKOTA
OFFICE OF THE STATE AUDITOR
STATE CAPITOL
600 E. BOULEVARD AVENUE - DEPT. 117
BISMARCK, NORTH DAKOTA 58505

Transmittal Letter

February 24, 2012

The Honorable Jack Dalrymple, Governor
Members of the North Dakota Legislative Assembly
Carol Olson, Executive Director, Department of Human Services

We are pleased to submit this audit of the Department of Human Services for the biennium ended June 30, 2011. This audit resulted from the statutory responsibility of the State Auditor to audit or review each state agency once every two years. The same statute gives the State Auditor the responsibility to determine the contents of these audits.

In determining the contents of the audits of state agencies, the primary consideration was to determine how we could best serve the citizens of the state of North Dakota. Naturally we determined financial accountability should play an important part of these audits. Additionally, operational accountability is addressed whenever possible to increase efficiency and effectiveness of state government.

The in-charge auditor for this audit was Michael Schmitcke, CPA, and Cindi Pedersen, CPA, was the audit manager. Inquiries or comments relating to this audit may be directed to the audit manager by calling (701) 328-2241. We wish to express our appreciation to Director Olson and her staff for the courtesy, cooperation, and assistance they provided to us during this audit.

Respectfully submitted,

A handwritten signature in cursive script that reads "Bob Peterson".

Robert R. Peterson
State Auditor

Executive Summary

Introduction

The Department of Human Services is an umbrella agency headed by Executive Director Carol Olson who was appointed by the Governor. The Department is organized into three major subdivisions consisting of Field Services, Program and Policy Management, and Managerial Support.

The Legislative Audit and Fiscal Review Committee (LAFRC) requests that certain items be addressed by auditors performing audits of state agencies. Those items and the Office of the State Auditor's response are noted below.

Responses to LAFRC Audit Questions

1. What type of opinion was issued on the financial statements?

Financial statements were not prepared by the Department of Human Services in accordance with generally accepted accounting principles so an opinion is not applicable. The agency's transactions were tested and included in the state's basic financial statements on which an unqualified opinion was issued.

2. Was there compliance with statutes, laws, rules, and regulations under which the agency was created and is functioning?

Yes.

3. Was internal control adequate and functioning effectively?

Other than our findings addressed on pages 15-21 we determined internal controls were adequate.

4. Were there any indications of lack of efficiency in financial operations and management of the agency?

No.

5. Has action been taken on findings and recommendations included in prior audit reports?

Except "Control/Fraud Risk Assessment Activities" as shown on page 26, the Department of Human Services has implemented all recommendations included in the prior audit report.

6. Was a management letter issued? If so, provide a summary below, including any recommendations and the management responses.

Yes, a management letter was issued and is included on page 27 of this report, along with management's response.

LAFRC Audit Communications

7. *Identify any significant changes in accounting policies, any management conflicts of interest, any contingent liabilities, or any significant unusual transactions.*

There were no significant changes in accounting policies, no management conflicts of interest were noted, no contingent liabilities were identified or significant unusual transactions.

8. *Identify any significant accounting estimates, the process used by management to formulate the accounting estimates, and the basis for the auditor's conclusions regarding the reasonableness of those estimates.*

The Department of Human Services' financial statements do not include any significant accounting estimates.

9. *Identify any significant audit adjustments.*

Significant audit adjustments were not necessary.

10. *Identify any disagreements with management, whether or not resolved to the auditor's satisfaction relating to a financial accounting, reporting, or auditing matter that could be significant to the financial statements.*

None.

11. *Identify any serious difficulties encountered in performing the audit.*

None.

12. *Identify any major issues discussed with management prior to retention.*

This is not applicable for audits conducted by the Office of the State Auditor.

13. *Identify any management consultations with other accountants about auditing and accounting matters.*

None.

14. *Identify any high-risk information technology systems critical to operations based on the auditor's overall assessment of the importance of the system to the agency and its mission, or whether any exceptions identified in the six audit report questions to be addressed by the auditors are directly related to the operations of an information technology system.*

- ConnectND Finance
- Human Resource Management System (HRMS)
- Contract Information System
- AIMS (Advanced Institutional Management Software)
- FACSES (Fully Automated Child Support Enforcement System)
- LIHEAP (Low Income Home Energy Assistance Program)
- ROAP (Regional Office Automated Program)

- CCWIPS (Comprehensive Child Welfare Information Payment System)
- MMIS (Medicaid Management Information System)
- VISION
- TECS (Technical Eligibility Computer System)
- Child Care Assistance
- VRIS (Vocational Rehabilitation Information System)

Audit Objectives, Scope, and Methodology

Audit Objectives

The objectives of this audit of the Department of Human Services for the biennium ended June 30, 2011 were to provide reliable, audited financial statements and to answer the following questions:

1. What are the highest risk areas of the Department of Human Services' operations and is internal control adequate in these areas?
2. What are the significant and high-risk areas of legislative intent applicable to the Department of Human Services and are they in compliance with these laws?
3. Are there areas of the Department of Human Services' operations where we can help to improve efficiency or effectiveness?

Audit Scope

This audit of the Department of Human Services is for the biennium ended June 30, 2011. We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

The Department of Human Services has its central office in the Capitol, eight regional human service centers, eight regional child support enforcement units, the State Hospital in Jamestown, and the Developmental Center in Grafton. All of these entities were included in the audit scope.

Audit Methodology

To meet the objectives outlined above, we:

- Prepared financial statements from the legal balances on the state's accounting system tested as part of this audit and the audit of the state's Comprehensive Annual Financial Report and developed a discussion and analysis of the financial statements.
- Performed detailed analytical procedures including computer-assisted auditing techniques. These procedures were used to identify high-risk transactions and potential problem areas for additional testing.
- Tested internal control and compliance with laws and regulations which included selecting representative samples to determine if controls were operating effectively and to determine if laws were being followed consistently. Non-statistical sampling was used and the results were projected to the population. Where applicable, populations were stratified to ensure that particular groups within a population were adequately represented in the sample, and to improve efficiency by gaining greater control on the composition of the sample.

- Interviewed appropriate agency personnel.
- Queried the ConnectND (PeopleSoft) system. Significant evidence was obtained from ConnectND.
- Observed the Department of Human Services' processes and procedures.

In aggregate there were no significant limitations or uncertainties related to our overall assessment of the sufficiency and appropriateness of audit evidence.

Discussion and Analysis

The accompanying financial statements have been prepared to present the Department of Human Services' revenues and expenditures on the legal (budget) basis. The accompanying financial statements are not intended to be presented in accordance with generally accepted accounting principles (GAAP).

For the biennium ended June 30, 2011, operations of the Department of Human Services were primarily supported by federal funds. This is supplemented by appropriations from the general fund and fees credited to the agency's operating fund.

Financial Summary

Revenues consisted primarily of federal funds. Other revenues during the audited period included patient care and treatment fees, revenue from local governments, pharmacy sales, and concessions. Total revenues were \$827.53 million for the year ended June 30, 2011 as compared to \$744.39 million for the year ended June 30, 2010. The increase in federal revenue for the audited period reflects primarily a legislative increase to all providers of 6% effective July 1, 2010 which resulted in more drawdowns of federal revenue. There was also a \$17.38 million increase from June 30, 2010 to June 30, 2011 in Patient Care and Treatment revenue. The majority of this change was due to an increase in developmentally disabled provider audit settlements, hospital settlements, drug rebates, and estate collections, as well as the timing of 3rd party collections.

Total expenditures for the Department of Human Services were \$1.15 billion for the year ended June 30, 2011 as compared to \$1.06 billion for the prior year. Grants accounted for a majority of the increase in total expenditures for the audit period. The increase in grant expenditures was a result of the following:

- The legislature provided a 6% increase for all providers of services effective July 1, 2010. These providers receive grants from the Department for providing services to programs such as Medicaid and Foster Care.
- The Department continued to see an increase in the utilization of Medicaid services, specifically in the following areas: developmental disability grants, traditional medical grants, Children's Health Insurance Program premium payments, nursing homes, and basic care facilities.

The increase in expenditures for salaries and benefits reflected the general salary increases. All other expenditures remained fairly constant.

The Department of Human Services accounts for child support collections and remittances in an agency fund. Agency fund activity is not included in the financial statements in this report. For the audit period collections totaled \$226,938,238 and disbursements totaled \$226,491,482.

Analysis of Significant Variances - Budgeted and Actual Expenditures

The excess of Capital Assets Carryover appropriations over actual expenditures was due to the amount of money appropriated for the replacement of the Medicaid Management Information System (MMIS) in chapter 50 of the 2007 Session Laws. North Dakota Century Code section 54-44.1-11 allowed for the carryover of these funds into the biennium under audit. The estimated completion date of the new system has been delayed several times and as a result actual expenditures have been less than the amounts budgeted. Excess appropriations in the Grants HSC/Institutions line and Grants – Medical Assistance line were the result of less American Recovery and Reinvestment Act (ARRA) monies being spent during the biennium than was anticipated in the budgeting process.

Financial Statements

Statement of Revenues and Expenditures

	<u>June 30, 2011</u>	<u>June 30, 2010</u>
<u>Revenues and Other Sources:</u>		
Revenue from Federal Government	\$ 781,790,251	\$ 716,495,785
Patient Care and Treatment Fees	33,160,349	15,898,937
Revenue from Local Governments	9,938,610	9,732,834
Pharmacy Sales	648,395	766,859
Concessions and Miscellaneous Sales	356,135	228,472
Lease/Rent of Buildings and Land	345,714	339,326
Other Revenue	900,183	592,676
Transfers In	387,259	332,229
Total Revenues and Other Sources	<u>\$ 827,526,896</u>	<u>\$ 744,387,118</u>
<u>Expenditures and Other Uses:</u>		
Grants	\$ 929,964,931	\$ 848,636,432
Salaries and Benefits	130,693,270	124,695,329
Operating Fees and Services	35,933,238	33,290,657
IT - Data Processing and Communications	18,995,768	19,705,796
IT - Contractual Services	5,521,062	4,086,266
Lease/Rent of Buildings and Land	4,340,759	4,352,799
Repairs	3,695,123	2,907,261
Supplies	3,013,901	2,278,185
Fees – Professional Services	2,636,149	2,273,578
Travel	2,402,812	2,306,395
Medical, Dental, and Optical	2,328,927	2,169,945
Utilities	2,145,847	2,041,819
Food and Clothing	1,447,655	1,337,005
Equipment	1,380,772	1,269,119
Postage	1,123,676	962,170
Printing	758,937	611,151
Professional Development	632,954	571,297
Other Expenses	282,576	1,078,047
Transfers Out	2,289,061	2,574,002
Total Expenditures and Other Uses	<u>\$1,149,587,418</u>	<u>\$1,057,147,253</u>

Statement of Appropriations

For The Biennium Ended June 30, 2011

Expenditures by Line Item:	<u>Original Appropriation</u>	<u>Adjustments</u>	<u>Final Appropriation</u>	<u>Expenditures</u>	<u>Unexpended Appropriation</u>
Salaries and Wages	\$ 58,384,151	\$ 755,682	\$ 59,139,833	\$ 58,333,993	\$ 805,840
Operating Expenses	123,032,122	1,024,022	124,056,144	117,204,562	6,851,582
Capital Assets	13,000	161,170	174,170	173,882	288
Capital Assets Carryover		31,434,000	31,434,000	10,029,091	21,404,909
Grants HSC/Institutions	472,338,947	10,602,010	482,940,957	412,974,257	69,966,700
Grants-Medical Assistance	267,935,408	2,319,222	270,254,630	263,314,838	6,939,792
Totals	<u>\$ 2,287,745,951</u>	<u>\$ 64,949,096</u>	<u>\$ 2,352,695,047</u>	<u>\$2,206,625,557</u>	<u>\$146,069,490</u>
Expenditures by Source:					
General Fund	\$ 650,645,814	\$ 4,101,085	\$ 654,746,899	\$ 627,347,763	\$ 27,399,136
Other Funds	1,637,100,137	60,848,011	1,697,948,148	1,579,277,794	118,670,354
Totals	<u>\$ 2,287,745,951</u>	<u>\$ 64,949,096</u>	<u>\$ 2,352,695,047</u>	<u>\$2,206,625,557</u>	<u>\$146,069,490</u>

Appropriation Adjustments:

The \$755,682 increase to the Salaries and Wages line consisted of the following adjustments:

- \$583,674 - Authorized by House Bill 1015 of the 2009 Session Laws – Section 18, for market equity increases.
- \$19,579 - Approved by the Emergency Commission to accept federal funds from the U.S. Department of Health and Human Services, Office of Administration on Aging, for development of an Aging and Disability Resource Center (ADRC).

- \$121,519 - Authorized by House Bill 1012 of the 2009 Session Laws – Section 7, which allows the Department of Human Services to transfer amounts between appropriation lines without Emergency Commission approval.
- \$30,910 – Authorized by House Bill 1015 of the 2009 Session Laws – Section 10, increased general fund spending authority for the state student internship program.

The \$1,024,022 increase to the Operating Expenses line consisted of the following adjustments:

- \$207,000 - Approved by the Emergency Commission, increased spending authority to accept federal funds from the American Recovery and Reinvestment Act (ARRA).
- \$13,000 – Authorized by House Bill 1012 of the 2009 Session Laws - Section 7, which allows the Department of Human Services to transfer amounts between appropriation lines without Emergency Commission approval.
- \$183,192 - Approved by the Emergency Commission to accept federal funds from the U.S. Department of Health and Human Services, Office of Administration on Aging for the development of an Aging and Disability Resource Center (ADRC).
- \$795,000 - Approved by the Emergency Commission to accept federal funds from the American Recovery and Reinvestment Act (ARRA) for the Child Support program, per the provisions of House Bill 1487 of the 2009 Session Laws.
- (\$174,170) – Authorized by House Bill 1012 of the 2009 Session Laws - Section 7, which allows the Department of Human Services to transfer amounts between appropriation lines without Emergency Commission approval.

The \$161,170 increase to the Capital Assets line consisted of the following adjustments:

- (\$13,000) – Authorized by House Bill 1012 of the 2009 Session Laws - Section 7, which allows the Department of Human Services to transfer amounts between appropriation lines without Emergency Commission approval.
- \$174,170 – Authorized by House Bill 1012 of the 2009 Session Laws - Section 7, which allows the Department of Human Services to transfer amounts between appropriation lines without Emergency Commission approval.

The \$31,434,000 increase to the Capital Assets Carryover line consisted of the following adjustments:

- \$ 31,654,000 - Authorized by the Capital Construction Carryover Committee for the following purposes:
 - \$1,399,625 for the State Hospital;
 - \$20,100 for the Developmental Center; and
 - \$30,234,275 for the Medicaid Management Information System project.

- (\$220,000) – House Bill 1012 of the 2009 Session Laws - Section 18, authorized spending authority for the roof replacement at the State Hospital. This amount was moved to the HSC/Institutions line.

The \$10,602,010 increase to the Grants line consisted of the following adjustments:

- \$10,855,000 - Approved by the Emergency Commission to accept federal funds from the American Recovery and Reinvestment Act (ARRA) for the Temporary Assistance for Needy Families (TANF) program.
- (\$252,990) - Authorized by House Bill 1012 of the 2009 Session Laws - Section 7, which allows the Department of Human Services to transfer amounts between appropriation lines without Emergency Commission approval.

The \$2,319,222 increase to the HSC/ Institutions line consisted of the following adjustments:

- \$270,000 - Authorized by Senate Bill 2012 of the 2007 Session Laws – Section 3, for completing roof repairs at the State Hospital. House Bill 1012 of the 2009 Session Laws - Section 18, authorized the carryover of unspent general fund appropriations.
- \$2,066,326 - Authorized by House Bill 1015 of the 2009 Session Laws – Section 18, to provide equity increases.
- \$104,415 - Authorized by House Bill 1015 of the 2009 Session Laws - Section 1, for the State Student Internship Program.
- (\$121,519) - Authorized by House Bill 1012 of the 2009 Session Laws - Section 7, which allows the Department of Human Services to transfer amounts between appropriation lines without Emergency Commission approval.

The \$18,652,990 increase to the Grants - Medical Assistance Line consisted of the following adjustments.

- \$18,400,000 - Approved by the Emergency Commission to accept federal funds from the American Recovery and Reinvestment Act (ARRA) for the Medical Assistance Program per the provisions of House Bill 1487 of the 2009 Session Laws.
- \$252,990 - Authorized by House Bill 1012 of the 2009 Session Laws - Section 7, which allows the Department of Human Services to transfer amounts between appropriation lines without Emergency Commission approval.

Expenditures Without Appropriations Of Specific Amounts:

Conference fund has a continuing appropriation authorized by OMB Policy 211 (\$19,325 of expenditures for this biennium).

Insurance recoveries fund has a continuing appropriation authorized by NDCC section 54-44.1-09.1 (\$17,927.96 of expenditures for this biennium).

Child Support Disbursement Unit Fund has continuing appropriation authorized by NDCC 14-09-25(5) (\$226,491,482 of expenditures for this biennium).

Donor Implied Trust Fund (off PeopleSoft activity) had expenditures of \$46,577 for this biennium.

State Hospital Patient Welfare Fund (off PeopleSoft activity) had expenditures of \$530,219 for this biennium.

Developmental Center Residents Welfare Fund (off PeopleSoft activity) had expenditures of \$51,646 for this biennium.

Medical Escrow Account (off PeopleSoft activity) had expenditures of \$9,232 for this biennium.

Internal Control

In our audit for the biennium ended June 30, 2011, we identified the following areas of the Department of Human Services' internal control as being the highest risk:

Internal Controls Subjected to Testing:

- Controls surrounding the processing of revenues.
- Controls surrounding the processing of expenditures.
- Controls effecting the safeguarding of assets.
- Controls relating to compliance with legislative intent.
- Controls surrounding accounts receivable write-offs.
- Controls surrounding the Home and Community Based Care program.
- Controls surrounding the following critical information systems:
 - ConnectND (PeopleSoft) system
 - Contract information system
 - AIMS (Advanced Institutional Management Software)
 - FACES (Fully Automated Child Support Enforcement System)
 - LIHEAP (Low Income Home Energy Assistance Program)
 - ROAP (Regional Office Automated Program)
 - CCWIPS (Comprehensive Child Welfare Information Payment System)
 - MMIS (Medicaid Management Information System)
 - VISION
 - TECS (Technical Eligibility Computer System)
 - Child Care Assistance
 - VRIS (Vocational Rehabilitation Information System)

The criteria used to evaluate internal control are published in the publication *Internal Control – Integrated Framework* from the Committee of Sponsoring Organizations (COSO) of the Treadway Commission.

We gained an understanding of internal control surrounding these areas and concluded as to the adequacy of their design. We also tested the operating effectiveness of those controls we considered necessary based on our assessment of audit risk. We concluded that internal control was not adequate noting certain matters involving internal control and its operation that we consider to be significant deficiencies.

Auditors are required to report deficiencies in internal control that are significant within the context of the objectives of the audit. A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect (1) misstatements in financial or performance information, (2) violations of laws and regulations, or (3) impairments of effectiveness or efficiency of operations, on a timely basis. Considering both qualitative and quantitative factors, we identified the following significant deficiencies in internal control. We also noted other matters involving internal control that we have reported to management of the Department of Human Services in a management letter dated February 24, 2012.

Control/Fraud Risk Assessment Activities (Finding 11-1)

Condition:

The Department of Human Services did not complete a department-wide risk assessment to identify control weaknesses in the department's financial, compliance, and operational areas.

While the Department has started some fraud risk assessment work, the work plan to cover all divisions is spread over six years.

Criteria:

Office of Management and Budget Policy 216 and *Internal Control - Integrated Framework* published by the Committee of Sponsoring Organizations of the Treadway Commission (COSO) requires management to adequately design and monitor internal control. This includes having adequate risk assessment policies and procedures.

Cause:

Lack of resources dedicated to monitoring internal controls.

Effect or Potential Effect:

Without adequate risk assessment activities, fraud and excessive errors can occur without being prevented or detected by management.

Recommendation:

We recommend the Department of Human Services:

- Establish and perform control risk assessments, including a fraud risk assessment, on a biennial basis; and
- Design and document the necessary control activities to ensure that each significant risk and fraud exposure identified during the risk assessment process has been adequately addressed.

Department of Human Services Response:

The Department does not have staff resources to complete a department-wide risk assessment on a biennial basis; however, we will continue to perform assessments with the resources available.

Inadequate Controls Surrounding Revenue Collections (Finding 11-2)

Condition:

Internal controls surrounding the receipt of revenue at the Southeast, North Central, Badlands, Northwest, West Central, and Northeast Human Service Centers and the State Hospital are inadequate. One or more of the following weaknesses were identified at each entity:

- Receipts were not reconciled to deposits by an individual who does not have access to cash;
- Bank reconciliations were prepared by individuals with access to cash;
- Excessive number of individuals with access to cash; and
- A remittance list is not prepared at the time the mail is opened.

Criteria:

According to the Committee of Sponsoring Organizations (COSO) Internal Controls - Integrated Framework Executive Summary, properly designed segregation of duties requires segregation between individuals that initiate transactions, have access to cash, and perform reconciliation procedures.

Cause:

The internal controls developed by the human service centers and the State Hospital were not adequate.

Effect or Potential Effect:

Increased potential for fraud and/or error to occur and go undetected.

Recommendation:

We recommend the Department of Human Services ensure:

- Receipts are reconciled to deposits by an individual who does not have access to cash;
- Bank reconciliations are prepared by individuals who do not have access to cash;
- Access to cash is properly limited; and
- Remittance lists are prepared at the time the mail is opened.

Department of Human Services Response:

The Department will enhance procedures surrounding revenue collections.

Provider Enrollment Controls Weakness (Finding 11-3)

Condition:

The Department of Human Services (DHS) does not have controls in place to ensure out-of-state providers meet the prescribed health and safety standards.

Criteria:

Title 42 of the Code of Federal Regulations, Part 442 requires that state agencies ensure hospitals, nursing facilities, and intermediate care facilities for the mentally retarded that serve Medicaid patients meet the prescribed health and safety standards.

Cause:

The Department did not implement this prior Single Audit finding.

Effect or Potential Effect:

As certain providers are not being reviewed for health and safety standards, the Department runs the risk of paying ineligible providers, which would also be a violation of federal law.

Recommendation:

We recommend the Department of Human Services implement controls to ensure out-of-state providers meet the prescribed health and safety standards.

Department of Human Services Response:

42 CFR 455.410 became effective February 2, 2011 and allows the State Medicaid agency to rely on the results of the provider screening completed by Medicare or another Medicaid/CHIP Agency and does not require the Medicaid agency to provide additional enrollment/re-enrollment screening. The Department is releasing Request for Proposals to secure a vendor(s) who will check the status of all out of state enrolled providers monthly to ensure the licensure of the out of state licensing agency remains in force and upon enrollment and re-enrollment to ensure their enrollment as a Medicare provider, or as a Medicaid/CHIP provider of another state remains in force.

Lack of Internal Controls at State Hospital's Commissary (Finding 11-4)

Condition:

The following internal control weaknesses were identified at the State Hospital's commissary:

- No control to ensure that all inventory purchases are received at the commissary.
- No independent reconciliation of till tapes to the bank statements.
- An analysis of revenues and expenditures is not performed.
- No written pricing policy.
- Inventory disposals are not tracked and approved.

Criteria:

According to the Committee of Sponsoring Organizations (COSO) Internal Controls and Control Activities, internal control is a process designed to provide reasonable assurance regarding the achievement of objectives in effectiveness and efficiency of operations, reliability of financial reporting, and compliance with applicable laws and regulations.

Cause:

The risks associated with the cash collections and inventory transactions made at the commissary were not adequately assessed by management.

Effect or Potential Effect:

The commissary recorded approximately \$300,000 of sales during the audit period, with the majority of collections being cash. The significant control weaknesses noted exposed cash and inventory to theft and fraud.

Recommendation:

We recommend the Department of Human Services develop internal controls to ensure:

- All inventory purchased is received by the commissary;
- The till tapes are independently reconciled to the bank statements;
- Revenues and expenditures are analyzed periodically;
- A written pricing policy is developed; and
- Inventory disposals are tracked and approved.

Department of Human Services Response:

The Department has developed internal controls surrounding the commissary activities.

Financial Reporting Errors (Finding 11-5)

Condition:

Financial data submitted by the Department of Human Services for preparation of the state's Comprehensive Annual Financial Report (CAFR) contained misstatements of approximately \$2.7 million for fiscal year 2010 and \$9.6 million for fiscal year 2011.

Criteria:

The Office of Management and Budget's CAFR Closing Manuals outline the requirements for submitting financial information.

Cause:

Certain controls established by the Department of Human Services are not operating effectively to help ensure the accuracy of financial information submitted to the Office of Management and Budget for CAFR reporting purposes.

Effect or Potential Effect:

Increased risk of material misstatement in financial statement reporting.

Recommendation:

We recommend the Department of Human Services ensure the financial data prepared for the State's Comprehensive Annual Financial Report is accurate.

Department of Human Services Response:

The Department will continue to strive to submit accurate data for the CAFR.

Lack of Child Care Assistance Controls (Finding 11-6)

Condition:

The procedures used by the Department to ensure Child Care Assistance payments are proper and made to eligible individuals are insufficient. The following weaknesses were noted:

- Internal controls are not sufficient to ensure case information and payment amounts are properly entered into the Child Care Assistance system;
- No independent review of over-payments and under-payments identified is done to ensure the actions taken by caseworkers were appropriate;
- Information provided by recipients is not verified using an external source when the recipient is receiving Child Care to attend college or seek employment when the recipient is not enrolled in another assistance program such as TANF;
- Errors detected during case reviews are documented but not in a way that would allow central office personnel to recognize unusual or suspicious patterns that may signal fraud and abuse;
- Support for discrepancies between the total amount of Child Care Assistance payments recorded on the Child Care Assistance system and PeopleSoft had to be recreated as original documentation was not maintained;
- Adjustments to ages of children can be made in the Child Care Assistance system to bring a child beneath the maximum eligible age of 13; and
- The number of case reviews performed monthly was considered insufficient and would not adequately mitigate the weaknesses noted above.

Criteria:

The Committee of Sponsoring Organizations of the Treadway Commission (COSO) Internal Control - Integrated Framework states that control activities are the policies and procedures that help ensure management directives are carried out. They help ensure the necessary actions are taken to address risks to achievement of the entity's objectives. Control activities occur throughout the organization, at all levels and in all functions. They include a range of activities such as approvals and segregation of duties.

Cause:

The information system used by the Department of Human Services to track eligibility and process payments for the Child Care Assistance program is outdated. This limits the ability of the Department to design and implement the proper internal controls.

Effect or Potential Effect:

There is potential for errors going undetected and fraud and/or fraudulent behavior.

Recommendation:

We recommend the Department of Human Services develop controls in the Child Care Assistance program to ensure proper payments are made to eligible individuals.

Department of Human Services Response:

The Department will continue to enhance procedures surrounding the Child Care Assistance Program.

Compliance With Legislative Intent

In our audit for the biennium ended June 30, 2011, we identified and tested the Department of Human Services' compliance with legislative intent for the following areas we determined to be significant and of higher risk of noncompliance:

- Compliance with appropriation laws (2009 Session Laws):
 - \$8.5 million Bank of North Dakota loan authorization related to medical assistance grants for medical services, long-term care, and developmental disabilities services (chapter 12, section 4).
 - Line item transfers in excess of \$50,000 reported to budget section (chapter 12, section 7).
 - \$4,124,506 appropriated from the Health Care Trust Fund for nursing facilities (chapter 12, section 8).
 - \$5,512,441 from the general fund, \$800,000 from the Health Care Trust Fund, \$11,665,072 from federal funds were appropriated for salary and benefit increases at basic care and skilled nursing care facilities (chapter 12, section 11).
 - \$7,086,807 from the general fund and \$14,552,299 from the federal fund were appropriated for salary and benefit increases for developmental disability providers (chapter 12, section 12).
 - \$400,000 appropriated from the general fund for providing supplemental payments to critical access hospitals (chapter 12, section 14).
 - \$270,000 carryover appropriation for roof repairs at the State Hospital (chapter 12, section 18).
 - \$100,000 appropriated from federal funds to inform the public about the alternatives-to-abortion program (chapter 412, section 3).
 - \$100,000 from the general fund and \$100,000 from federal funds were appropriated to enter a contract to study the rate setting structure used to reimburse public and private providers who serve medically fragile and behaviorally challenged individuals (chapter 409, section 1).
 - \$3,644,000 appropriated from federal funds to provide training, quality improvement, technical assistance, and capacity building for the early childhood care and education workforce (chapter 425, section 2).
 - \$350,000 appropriated from the general fund to contract with a statewide charitable food recovery and distribution organization to develop and implement new methods of delivering charitable food assistance services in under-served counties (chapter 416, section 2).
 - \$549,938 appropriated from the general fund for reimbursing expenses of locally administered economic assistance programs in counties that contain federally recognized Indian reservation land (chapter 410, section 2).
 - \$200,000 appropriated for DHS to issue a grant to a facility which incurs a transfer of the location of all the facility's beds and a change of operator before June 1, 2009, for costs associated with the remodeling of the facility (chapter 408, section 1).

- \$28,761 appropriated from the general fund and \$337,144 from federal funds for the purpose of funding a special care rate for qualifying nursing homes (chapter 432, section 1).
- \$330,000 appropriated from the general fund for the purpose of providing services to individuals with traumatic brain injury (chapter 418, section 9).
- Compliance with a requirement to ensure nurse practitioners are considered primary care providers and to ensure DHS submitted a state plan amendment to the federal agency within 30 days of August 1, 2009 (2009 Session Laws, chapter 429, sections 1 & 2).
- Compliance with a requirement to adopt guidelines for case referrals to children's advocacy centers (NDCC 50-25.1-05).
- Compliance with a requirement to award a contract for outreach services for the children's health insurance program (2009 Session Laws, chapter 12, section 17).
- Establishment of an autism spectrum disorder task force and state autism spectrum disorder plan by July 1, 2010 (2009 Session Laws, chapter 413, section 1).
- Compliance with a requirement to review the audit and reimbursement process and reconsideration of the 95% occupancy rule for developmental disability providers (2009 Session Laws, chapter 417, section 1).
- Compliance with a requirement to create a program for services to transition-aged youth at risk (2009 Session Laws, chapter 415, section 1).
- Compliance with a requirement for DHS to prepare a comprehensive human services plan on a biennial basis (NDCC section 50-06.2-03).
- Proper use of the following legally restricted funds:
 - Employment of People with Disabilities Fund (NDCC 39-01-15 (5))
 - North Dakota Health Care Trust Fund (NDCC 50-30-02)
 - Children's Trust Fund (NDCC 50-27-02)
 - Child Support Disbursement Unit Fund (NDCC 14-09-25)
 - Human Services Donor Implied Trust Fund (59-21)
- Proper use of the State Treasurer (State Constitution, article X, section 12).
- Compliance with OMB's Purchasing Procedures Manual.
- Travel-related expenditures are made in accordance with OMB policy and state statute.
- Proper use of outside bank accounts, petty cash funds, and proper authority for investments outside the Bank of North Dakota.
- Adequate blanket bond coverage of employees (NDCC section 26.1-21-08).
- Compliance with fixed asset requirements including record-keeping, lease and financing arrangements in budget requests, and lease analysis requirements.
- Compliance with payroll-related laws including statutory salaries for applicable elected and appointed positions, and certification of payroll.

The criteria used to evaluate legislative intent are the laws as published in the *North Dakota Century Code* and the *North Dakota Session Laws*.

Government Auditing Standards require auditors to report all instances of fraud and illegal acts unless they are inconsequential within the context of the audit objectives. Further, auditors are

required to report significant violations of provisions of contracts or grant agreements, and significant abuse that has occurred or is likely to have occurred.

The results of our tests disclosed no instances of noncompliance that are required to be reported under *Government Auditing Standards*. Thus, we concluded there was compliance with the legislative intent identified above.

While we did not find any items that were required to be reported in accordance with *Government Auditing Standards*, we noted certain inconsequential or insignificant instances of non-compliance that we have reported to management of the Department of Human Services in a management letter dated February 24, 2012.

Operations

This audit did not identify areas of the Department of Human Services operations where we determined it was practical at this time to help to improve efficiency or effectiveness.

Prior Recommendations Not Implemented

Prior recommendations have been implemented with the exception of the following:

Control/Fraud Risk Assessment Activities (Finding 09-1)

Recommendation:

We recommend the Department of Human Services:

- Establish and perform a control risk assessment including a fraud risk assessment on a recurring basis; and
- Design and document the necessary control activities to ensure that each of the significant control risks and fraud exposures identified during the risk assessment process has been adequately mitigated.

Status:

Not implemented. See recommendation 11-1 on page 15.

Management Letter (Informal Recommendations)

February 24, 2012

Ms. Carol Olson, Executive Director
Department of Human Service
600 E Boulevard Avenue
Bismarck, ND 58505

Dear Executive Director Olson:

We have performed an audit of the Department of Human Services for the biennium ended June 30, 2011, and have issued a report thereon. As part of our audit, we gained an understanding of the Department of Human Services' internal control structure to the extent we considered necessary to achieve our audit objectives. We also performed tests of compliance as described in the same report.

Our audit procedures are designed primarily to enable us to report on our objectives including those related to internal control and compliance with laws and regulations and may not bring to light all weaknesses in systems and procedures or noncompliance with laws and regulations which may exist. We aim, however, to use our knowledge of your organization gained during our work to make comments and suggestions which we hope will be useful to you.

In connection with the audit, gaining an understanding of the internal control structure, and tests of compliance with laws and regulations referred to above, we noted certain conditions we did not consider reportable within the context of your audit report. These conditions relate to areas of general business practice or control issues that have no significant bearing on the administration of federal funds. We do, however, want to present our recommendations to you for your consideration and whatever follow-up action you consider appropriate. During the next audit we will determine if these recommendations have been implemented, and if not, we will reconsider their status.

The following present our informal recommendations.

CASH

Informal Recommendation 11-1: We recommend the Developmental Center ensure the individual responsible for preparing billings, updating account receivable, and recording write-offs or adjustments for adaptive equipment does not have access to cash.

PAYROLL

Informal Recommendation 11-2: We recommend the Developmental Center ensure computer access privileges are properly restricted to those who need access to complete their job duties and the State Hospital ensure computer access rights for former employees are properly terminated.

Informal Recommendation 11-3: We recommend the North Dakota State Hospital and Developmental Center establish procedures to ensure all payroll adjustments are properly approved and supported.

Informal Recommendation 11-4: We recommend the Department of Human Services strengthen internal controls to ensure:

- Service awards are given to the correct individuals and for the correct amounts in compliance with DHS policy;
- A policy is developed to identify procedures for repayment of bonuses due back to DHS; and
- Performance bonuses are given in compliance with NDCC 54-06-30.

LEGISLATIVE INTENT

Informal Recommendation 11-5: We recommend the Department of Human Services comply with NDCC 50-06.2-03 (2) by preparing a comprehensive human services plan.

Informal Recommendation 11-6: We recommend the Department of Human Services implement procedures to ensure any future state plan amendments mandated by state law are submitted within the required time frame.

Informal Recommendation 11-7: We recommend the State Hospital develop procedures to pay interest earned on the Rental Trust account in accordance with NDCC 47-16-07.1.

ACCOUNTS PAYABLE/EXPENDITURES

Informal Recommendation 11-8: We recommend the Department of Human Services ensure all individual purchase card statements are reconciled to the company statement by a non-cardholder.

Informal Recommendation 11-9: We recommend the Department of Human Services follow OMB's procurement requirements when making purchases.

Informal Recommendation 11-10: We recommend the North Dakota State Hospital adequately segregate check writing, check signing, check mailing, and check register duties surrounding the clearing account.

Informal Recommendation 11-11: We recommend the Department of Human Services:

- Code expenditures using PeopleSoft coding that is consistent with the nature of the expenditures;
- Retain the original receipts/invoices to properly support the expenditure; and
- Develop procedures to ensure sales tax is not paid on purchases.

INVENTORY

Informal Recommendation 11-12: We recommend the Department of Human Services ensure:

- Drug inventories at the human service centers are randomly spot checked by an independent individual; and
- Year-end inventories taken are observed by an independent individual.

Informal Recommendation 11-13: We recommend the State Hospital establish controls surrounding Central Service and Central Receiving inventory to ensure:

- Inventory records are kept by an individual who is not authorized to initiate requisitions on the Lawson System without proper approval; and
- Requisitions are signed by the requester upon receipt of the inventory.

PERVASIVE CONTROLS

Informal Recommendation 11-14: We recommend the Department of Human Services include a provision for full, fair, accurate, timely, and understandable disclosure in reports and documents in their Code of Conduct Policy.

INFORMATION SYSTEMS

Informal Recommendation 11-15: We recommend the Department of Human Services ensure:

- Central Office employees do not have access to create Low Income Home Energy Assistance Program (LIHEAP) cases;
- The director of the LIHEAP program does not have access to update case files; and
- The director of the LIHEAP program monitors and approves all case updates made by the assistant.

Informal Recommendation 11-16: We recommend the Department of Human Services ensure access rights to make adjustments to the payment rate tables in the Comprehensive Child Welfare Information Payment System (CCWIPS) program are limited to those individuals that need access to perform their job duties.

Informal Recommendation 11-17: We recommend the Department of Human Services' Child Support Division expand its current process to ensure debt adjustments and refunds are sufficiently reviewed by an individual independent of preparation.

FIXED ASSETS

Informal Recommendation 11-18: We recommend the Department of Human Services ensure:

- Individuals responsible for taking physical inventory do not have access to update computerized fixed asset records;
- A written policy for the deletion of fixed assets is created; and
- Access to computerized fixed asset records is limited to one individual at each human service center, Developmental Center, and State Hospital.

Management of the Department of Human Services agreed with these recommendations.

I encourage you to call myself or an audit manager at 328-2241 if you have any questions about the implementation of recommendations included in your audit report or this letter.

Sincerely,

A handwritten signature in cursive script that reads "Michael W. Schmitcke".

Michael W. Schmitcke, CPA
Auditor in-charge

You may obtain audit reports on the internet at:

www.nd.gov/auditor/

or by contacting the
Division of State Audit

Office of the State Auditor
600 East Boulevard Avenue – Department 117
Bismarck, ND 58505-0060

(701) 328-2241