AUDIT REPORT

Department of Finance and Administration

May 2008

STATE OF TENNESSEE
COMPTROLLER OF THE TREASURY

Department of Audit

Division of State Audit

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STATE OF TENNESSEE

COMPTROLLER OF THE TREASURY

State Capitol
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John G. Morgan
Comptroller

May 22, 2008

The Honorable Phil Bredesen, Governor
and
Members of the General Assembly
State Capitol
Nashville, Tennessee 37243
and
The Honorable Dave Goetz, Commissioner
Department of Finance and Administration
State Capitol
Nashville, Tennessee 37243

Ladies and Gentlemen:

Transmitted herewith is the financial and compliance audit of the Department of Finance and Administration for the period April 1, 2005, through May 31, 2007.

The review of internal control and compliance with laws, regulations, and provisions of contracts and grant agreements resulted in certain findings which are detailed in the Objectives, Methodologies, and Conclusions section of this report.

Sincerely,

John G. Morgan

John G. Morgan
Comptroller of the Treasury

JGM/sah
07/075

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COMPTROLLER OF THE TREASURY
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August 17, 2007

The Honorable John G. Morgan
Comptroller of the Treasury
State Capitol
Nashville, Tennessee 37243

Dear Mr. Morgan:

We have conducted a financial and compliance audit of selected programs and activities of the Department of Finance and Administration for the period April 1, 2005, through May 31, 2007.

We conducted our audit in accordance with *Government Auditing Standards*, issued by the Comptroller General of the United States. These standards require that we obtain an understanding of internal control significant to the audit objectives and that we design the audit to provide reasonable assurance of the Department of Finance and Administration's compliance with laws, regulations, and provisions of contracts and grant agreements significant to the audit objectives. Management of the Department of Finance and Administration is responsible for establishing and maintaining effective internal control and for complying with applicable laws, regulations, and provisions of contracts and grant agreements.

Our audit disclosed certain findings which are detailed in the Objectives, Methodologies, and Conclusions section of this report. The department's administration has responded to the audit findings; we have included the responses following each finding. We will follow up the audit to examine the application of the procedures instituted because of the audit findings.

We have reported other less significant matters involving the Department of Finance and Administration's internal control to the department's management in a separate letter.

Sincerely,

Arthur A. Hayes, Jr., CPA
Director

AAH/sah

State of Tennessee

Audit Highlights

Comptroller of the Treasury Division of State Audit

Financial and Compliance Audit
Department of Finance and Administration
May 2008

AUDIT SCOPE

We have audited the Department of Finance and Administration for the period April 1, 2005, through May 31, 2007. Our audit scope included a review of internal control and compliance with laws, regulations, and provisions of contracts and grant agreements in the areas of the Division of Mental Retardation Services' contract management, conflict-of-interest policy, travel claims, personnel procedures, and the developmental centers' operations; payment card usage; the Office of Business and Finance; and miscellaneous issues. The audit was conducted in accordance with *Government Auditing Standards*, issued by the Comptroller General of the United States. Tennessee statutes, in addition to audit responsibilities, entrust certain other responsibilities to the Comptroller of the Treasury. Those responsibilities include serving as a member of the board of directors of the Local Education Insurance Committee, Local Government Insurance Committee, State Building Commission, State Insurance Committee, Information Systems Council, and TennCare Prescription Drug Committee; approving accounting policies of the state as prepared by the state's Department of Finance and Administration; approving certain state contracts; participating in the negotiation and procurement of services for the state; providing support staff to various legislative committees and commissions; and developing policy guidelines for the overall management of the state's information systems.

AUDIT FINDINGS

The Division of Mental Retardation Services' Subrecipients Are Monitored by Internal Audit; However, Improvements to That Process Along With Changes to the Provider Manual Could Further Reduce the Risk of Fraud, Waste, and Abuse
Our review of the monitoring process found areas where improvements should be made in the internal auditors' methodologies, in the Provider Manual, and in the resolution of questioned costs (page 9).

The Division of Mental Retardation Services Still Had Inadequate Controls Over the Contract With the Community Services Network of West Tennessee, Hampering the Division's Ability to Properly Administer the Contract**
The division again failed to follow the contract provisions and still had not resolved a potential conflict of interest pertaining to a CSN board member. The division also failed to reconcile claims payments maintained by

CSN to the amounts withdrawn from the division's account (page 14).

The Division of Mental Retardation Services Has Still Failed to Collect Available Federal Reimbursement for Waiver Services, Thus Costing State Taxpayers Millions of Dollars**

As of May 15, 2007, the division had accumulated approximately $23,000,000 of denied and pended claims for fiscal year 2006 waiver services paid in the period September 2005 to August 2006. The division had also accumulated approximately $8,000,000 of denied and pended claims for the first quarter of fiscal year 2007 waiver services paid in the period September 2006 to November 2006 (page 17).

The Division of Mental Retardation Services Has Again Arbitrarily Paid for Housing Subsidies Without Rules for Eligibility*

There were no written policies or procedures to provide the housing subsidies equitably to all eligible clients or to regulate the total state funds spent to provide this supplement. The division paid rents that appeared much higher that those estimated by the U.S. Department of Housing and Urban Development on several properties (page 21).

The Division of Mental Retardation Services Has Still Failed to Strengthen Controls Over the Payment Process and Its Claim System, Community Services Tracking; Thus, It Overpaid Providers Hundreds of Thousands of Dollars and Created a Fertile Ground for Fraudulent Transactions*

Multiple security controls were weak and access capabilities of the employees were inappropriate. There was not an effective control mechanism for detecting and correcting data-entry mistakes and billing errors involving service-contract payments. In addition, the division did not maintain adequate and updated system documentation (page 25).

The Division of Mental Retardation Services Still Had Improper Employer-Employee Relationships, Raising Serious Policy and Legal Issues**

Management contracted with agencies to provide individuals that were directly supervised by state employees and contract employees that supervised state employees. These contract employees functioned much in the same manner as state employees (page 30).

Internal Control Over Resident Trust Funds at Clover Bottom Developmental Center Was Still Inadequate, Increasing the Risk for Misuse or Loss*

Employees did not always follow established procedures for purchases made on behalf of the residents. There was cash outstanding from the funds for excessive periods. Some purchased items were not entered into the residents' inventory records (page 33).

Controls Over Resident Trust Funds at Greene Valley Developmental Center Were Inadequate, Increasing the Risk for Misuse or Loss

Employees did not return unspent residents' funds to the center's accounting department within the required time frame and did not place funds in the safes at the homes when the funds were not being used to fill the residents' requests (page 35).

The Department of Finance and Administration, Including the Division of Mental Retardation Services, Failed to Promptly Terminate the Service for Unused Telephone Lines, Resulting in Estimated Unnecessary Costs to the State of Over $3,300 per Month

The Department of Finance and Administration, excluding the Division of Mental Retardation Services, made payments for 89 unused telephone lines which totaled $2,218 per month. Additional payments for telephone lines unused by the Division of Mental Retardation Services were estimated to be over $1,100 per month (page 40).

Management of the Division of Mental Retardation Services Has Not Fulfilled Its Responsibility to Formally Assess the Division's Risks of Errors, Fraud, Waste, and Abuse

Our discussions with management of the division disclosed that they have not fulfilled their responsibility to formally assess the division's risks of errors, fraud, waste, and abuse and to document the risk assessment as of the end of our audit period, May 31, 2007 (page 41).

* This finding is repeated from the prior audit.

** This finding is repeated from prior audits.

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Department of Finance and Administration

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INTRODUCTION

POST-AUDIT AUTHORITY

This is the report on the financial and compliance audit of the Department of Finance and Administration. The audit was conducted pursuant to Section 4-3-304, *Tennessee Code Annotated*, which requires the Department of Audit to "perform currently a post-audit of all accounts and other financial records of the state government, and of any department, institution, office, or agency thereof in accordance with generally accepted auditing standards and in accordance with such procedures as may be established by the comptroller."

Section 8-4-109, *Tennessee Code Annotated*, authorizes the Comptroller of the Treasury to audit any books and records of any governmental entity that handles public funds when the Comptroller considers an audit to be necessary or appropriate.

BACKGROUND

The mission of the Department of Finance and Administration is to provide financial and administrative support services for all facets of state government. The business, finance, and managerial functions of state government are centralized here. The department prepares and executes the state budget, accounts for state revenues and expenditures, operates a central data processing center, plans and reviews construction and alteration of state buildings, and controls state-owned and leased property. Also, as a result of Executive Orders, the department is responsible for the state's TennCare program and the state's Mental Retardation Services, including its developmental centers.

In addition to TennCare and the Division of Mental Retardation Services, the Department of Finance and Administration contains 11 divisions: Accounts, Administration, Benefits Administration, Budget, Enterprise Resource Planning, Health Planning, Office for Information Resources, Office of the Inspector General, Real Property Administration, Resource Development and Support, and Shared Services Solutions.

The Division of Mental Retardation Services is responsible for providing services to Tennesseans of all ages with mental retardation and other developmental disabilities. The division oversees three regional offices which coordinate services to individuals in the community, and the operation of the three developmental centers (Arlington in the west, Clover Bottom in the middle, and Greene Valley in the east.)

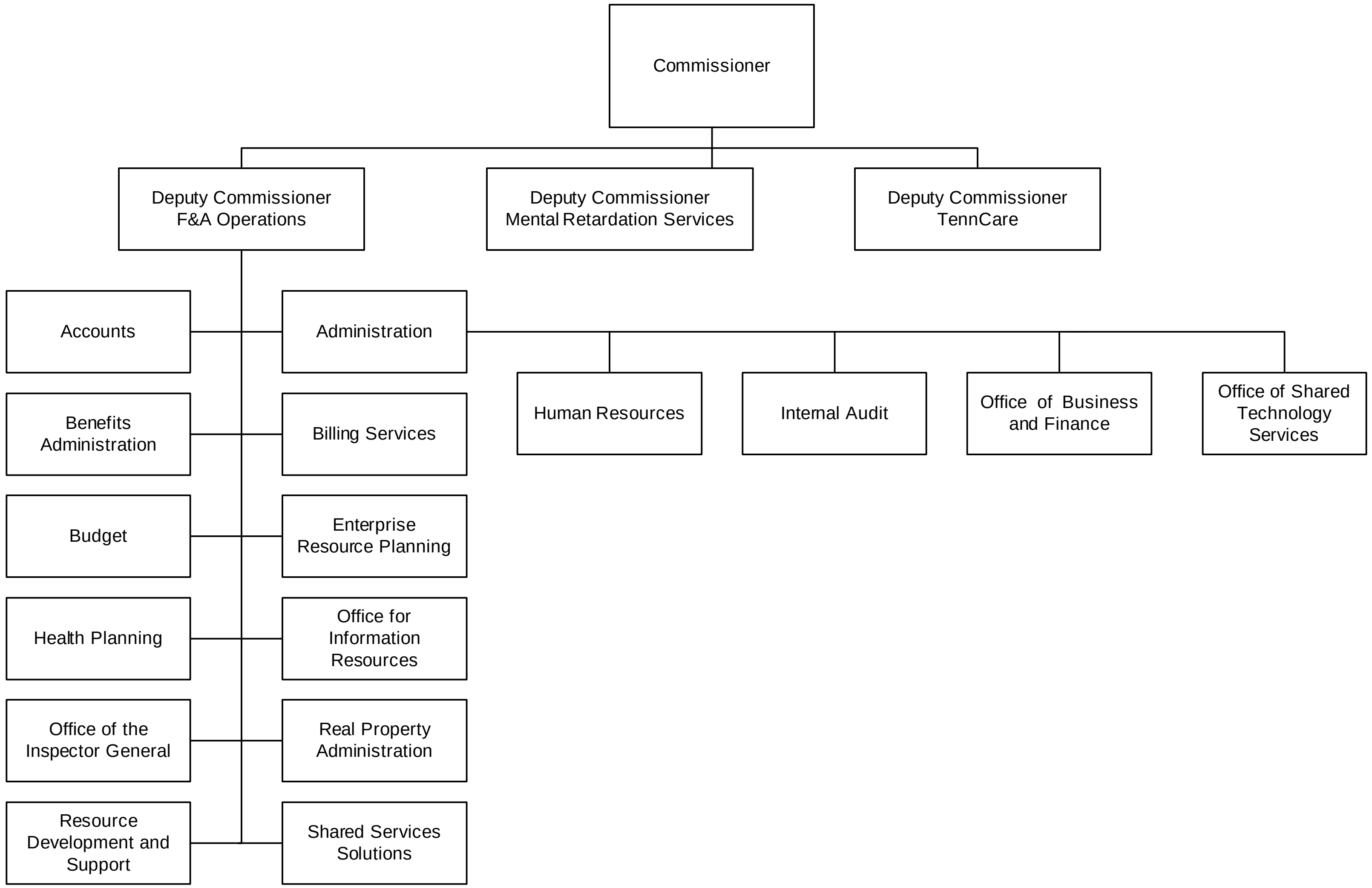
The Division of Mental Retardation Services currently serves 561 individuals in the developmental centers and 7,791 individuals in the community. Of the total number in the community, 6,026 are served through the main Medicaid Home and Community Based Services waiver, 225 are served through the Arlington waiver, 993 are served through the Self Determination waiver, and 547 are funded by the state. As of June 30, 2007, there were 5,834 people on the waiting list for the waiver services. This includes individuals who are not currently receiving any services as well as those waiting for specifically requested services that are not yet available. The division currently operates under four court orders/agreements: *United States v. State of Tennessee* (Arlington Remedial Order), *People First v. Clover Bottom et al.* (Settlement Agreement), the Revised Consent Decree Governing TennCare Appeals (Grier Lawsuit), and *Beth Ann Brown et al. v. Tennessee Department of Finance and Administration* (Waiting List – Agreed Settlement currently being implemented).

Organization charts of the Department of Finance and Administration, the Division of Mental Retardation Services, and the Office of Business and Finance are on the following pages.

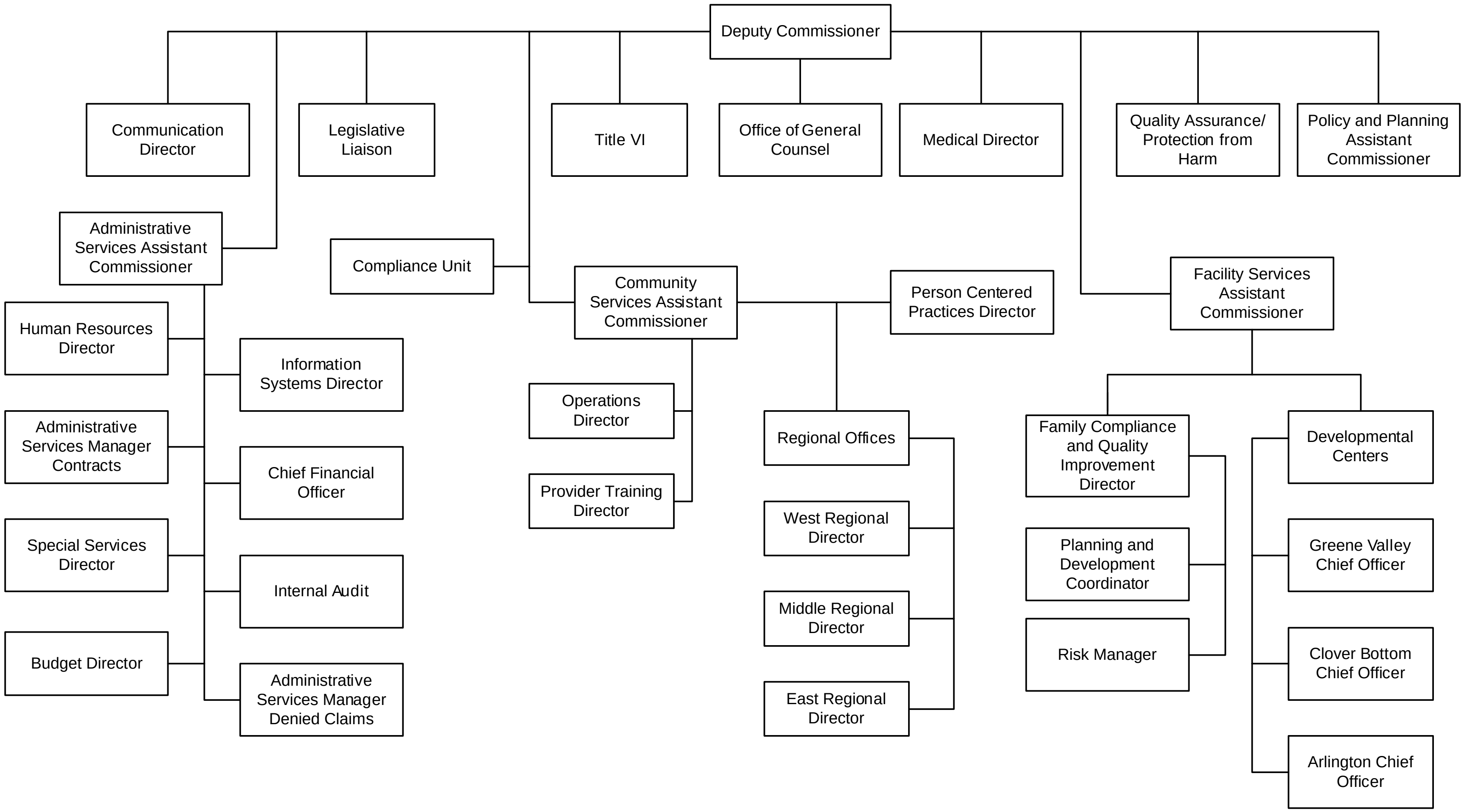
AUDIT SCOPE

We have audited the Department of Finance and Administration for the period April 1, 2005, through May 31, 2007. Our audit scope included a review of internal control and compliance with laws, regulations, and provisions of contracts and grant agreements in the areas of the Division of Mental Retardation Services' contract management, conflict-of-interest policy, travel claims, personnel procedures, and the developmental centers' operations; payment card usage; the Office of Business and Finance; and miscellaneous issues. This audit did not include certain other areas material to the *Tennessee Comprehensive Annual Financial Report* for the year ended June 30, 2006, and the Tennessee Single Audit for the same period. The results of our audits for those areas, including the Medical Assistance Program (Medicaid/TennCare) and the statewide controls administered by the Department of Finance and Administration, were reported in the *State of Tennessee Single Audit Report*. The audit was conducted in accordance with *Government Auditing Standards*, issued by the Comptroller General of the United States. Tennessee statutes, in addition to audit responsibilities, entrust certain other responsibilities to the Comptroller of the Treasury. Those responsibilities include serving as a member of the board of directors of the Local Education Insurance Committee, Local Government Insurance Committee, State Building Commission, State Insurance Committee, Information Systems Council, and TennCare Prescription Drug Committee; approving accounting policies of the state as prepared by the state's Department of Finance and Administration; approving certain state contracts; participating in the negotiation and procurement of services for the state; providing support staff to various legislative committees and commissions; and developing policy guidelines for the overall management of the state's information systems.

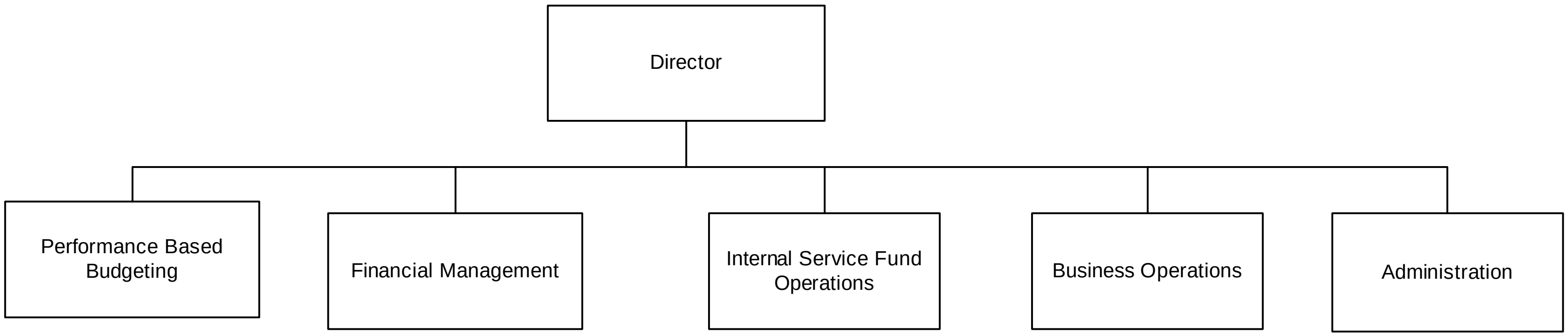
Department of Finance and Administration
Organization Chart



Division of Mental Retardation Services
Organization Chart



Finance and Administration
Office of Business and Finance
Organization Chart



PRIOR AUDIT FINDINGS

Section 8-4-109, *Tennessee Code Annotated*, requires that each state department, agency, or institution report to the Comptroller of the Treasury the action taken to implement the recommendations in the prior audit report. The Department of Finance and Administration filed its report with the Department of Audit on April 30, 2007. A follow-up of all prior audit findings was conducted as part of the current audit.

RESOLVED AUDIT FINDINGS

The current audit disclosed that the Department of Finance and Administration has corrected the previous audit findings concerning inadequate controls over other contracts, the lack of adequate controls over payment card usage, incomplete personnel files, inadequate recordkeeping for equipment at Arlington Developmental Center, and lack of an effective conflict-of-interest policy. The current audit also disclosed that the Department of Finance and Administration has strengthened the controls over employees' travel claims in the Division of Mental Retardation Services, in response to the special investigations finding noted in the previous audit report.

REPEATED AUDIT FINDINGS

The prior audit report also contained findings concerning inadequate controls over the contract with the Community Services Network of West Tennessee Inc., inadequate documentation for waiver services, not maximizing federal financial participation, payment of housing subsidies, inadequate controls over the Community Services Tracking system, improper employer-employee relationships, and inadequate controls over Clover Bottom Developmental Center trust funds. These findings had not been resolved and are repeated in the applicable sections of this report.

<u>Most Recent Audit Report</u>

Report number 06/083 – The Department of Finance and Administration's *Audit Results from the Comprehensive Annual Financial Report and Single Audit Procedures*, issued in April 2007, contained certain audit findings that were included in the *State of Tennessee Single Audit Report*. These findings were not relevant to our current audit, and, as a result, we did not pursue their status as a part of this audit.

OBJECTIVES, METHODOLOGIES, AND CONCLUSIONS

DIVISION OF MENTAL RETARDATION SERVICES' CONTRACT MANAGEMENT

The objectives of our review of the controls and procedures over contract management in the Division of Mental Retardation Services (DMRS) were to determine whether

- policies and procedures over service contracts were adequate, clear, and understood by employees, service providers, and other involved parties;
- sufficient monitoring of service contracts was performed;
- the monitoring was properly conducted;
- questioned costs were properly evaluated and resolved;
- clients' bank accounts and related transactions were properly managed by the providers;
- the provisions of the contract with the Community Services Network of West Tennessee (CSN) were reasonable and followed;
- payments to CSN were properly monitored and known questioned costs were properly resolved;
- clients receiving waiver services were eligible according to TennCare;
- internal control over reimbursement of federal financial participation from TennCare was adequate;
- policies and procedures for housing supplements were adequate; and
- internal controls related to the direct service provider payment system (Community Services Tracking) and the payment process were adequate.

We interviewed key personnel and reviewed rules and policies to gain an understanding of the division's procedures and controls over contract management. We reviewed the Provider Manual and interviewed personnel and providers to determine the adequacy and comprehensibility of the division's policies and procedures over service contracts. We obtained a list of monitoring reviews completed by DMRS' internal auditors from April 2005 through April 2007. We compared the number of the reviews completed to that of active service providers of the same period. We randomly selected and reviewed the working papers of 14 monitoring reviews to determine the adequacy of the samples and to determine whether the samples were reconciled to the records on the division's claim system, Community Services Tracking (CS Tracking). We reconciled all service charges reviewed by the internal auditors in these 14 monitoring reviews to the records on CS Tracking to determine whether or not these charges were later adjusted after being reviewed by the internal auditors. To review the monitoring work performed by the internal auditors, we selected and reexamined a nonstatistical sample of 60 contract service charges from 5 of the 14 monitoring reviews mentioned to determine whether our findings would be the same as the internal auditors' findings. We also analyzed and identified explanations for differences between our findings and those of the internal auditors to determine whether the monitoring reviews were properly conducted. We also followed up on how questioned costs found by the internal auditors were resolved.

For clients whose charges were included in the 60 contract service charges tested above and whose bank accounts were administered by the providers, we obtained and reviewed the monthly reconciliations and the related transactions to determine whether the reconciliations and the related transactions were adequately supported and proper.

We interviewed key personnel and reviewed contractual arrangements between DMRS and CSN. We also obtained and reviewed the working papers of the latest monitoring review on CSN completed by the division's internal auditors and reexamined the administrative, state-funded health and behavioral services, and waiver services expenses to determine whether our findings would be the same as the internal auditors' findings. We also analyzed and identified explanations for differences between our findings and those of the internal auditors to determine whether the monitoring reviews were properly conducted. We also followed up on how questioned costs found by the internal auditors were resolved.

For clients who received waiver services and were included in the CSN monitoring review or the five other monitoring reviews mentioned above, we determined whether the clients were active Medicaid recipients on TennCare's system.

To review the process for requesting federal financial participation through TennCare, we obtained the reconciliation schedule for waiver services paid from August 2005 to March 2007 maintained by the division. We verified the amounts of waiver services paid by the division to the claim payment history files generated from the division's claims payment system, CS Tracking. We also verified the amounts of waiver services reimbursed from TennCare to the State of Tennessee Accounting and Reporting System (STARS) and the remittance advices from TennCare. Next we computed the amounts of waiver services provided in the year ended June 30, 2006, and the first quarter of fiscal year 2007 that had not been reimbursed from TennCare as of May 2007. We also interviewed employees who were involved in the process for requesting federal financial participation through TennCare to seek explanations for denied or pended reimbursement claims.

We interviewed key officials about the housing supplements paid to clients to determine related policies and procedures. We obtained a listing of all housing supplement payments and summarized the payments by client and by service period to determine if any clients received more than one payment for a given service period. Furthermore, the listing was sorted by payment amount to determine the clients that received the highest dollar amounts per month of housing subsidies to determine the justification for such amounts.

Lastly, key officials were interviewed about the controls over direct service payments and the division's claims payment system, CS Tracking, to determine if controls over the system and the related process were adequate.

Based on our interviews and testwork, we determined that policies and procedures over service contracts were ambiguous and were not understood by employees, service providers, and other involved parties. Also, although the division's internal auditors performed sufficient monitoring, we determined that the monitoring process could be improved in five areas. In addition, although the division did seek recoveries of known questioned costs, the division failed to compare the levels of questioned costs among providers in order to identify repeated and serious instances of noncompliance. Weaknesses in policies and procedures and those in the monitoring process are detailed in finding 1. Based on the procedures performed, clients' accounts and transactions within the accounts were properly managed by the providers. Our review and testwork showed that contractual arrangements with CSN were weak and their provisions were not followed by the division, but CSN was properly monitored and known questioned costs were properly resolved. The CSN weaknesses are detailed in finding 2. The process for obtaining reimbursement of waiver services from TennCare was inadequate, and not all of the clients who received waiver services were eligible on TennCare's system. Weaknesses regarding the process for obtaining reimbursement of waiver services from Tenncare and the clients' eligibility are detailed in finding 3. Furthermore, policies and procedures for housing supplements were not adequate, as noted in finding 4. Also, multiple internal control deficiencies were noted in the CS Tracking system and the related payment process as detailed in finding 5.

1. <u>The Division of Mental Retardation Services' subrecipients are monitored by Internal Audit; however, improvements to that process along with changes to the Provider Manual could further reduce the risk of fraud, waste, and abuse</u>

Finding

Internal auditors in the Division of Mental Retardation Services (DMRS) conduct monitoring reviews of provider contracts on a regular basis as required by the Department of Finance and Administration's Policy 22, "Subrecipient Contract Monitoring." The objectives of the reviews typically include, among other things, the determination of whether costs and services were allowable and eligible and whether the providers were in compliance with contract provisions. Our review of this process found areas where improvements should be made in the internal auditors' methodologies, in the Provider Manual, and in the resolution of questioned costs.

<u>Internal Audit</u>

Although internal auditors performed sufficient monitoring and, in doing so, tested large enough samples, the monitoring process could be improved. Our review found that

1. Internal Audit didn't examine the best sources of evidence that were available to them,

2. the review performed by Internal Audit excluded payments resulting from the adjustment process,

3. Internal Audit did not perform procedures to determine whether billings exceeded the maximum total units allowed under the contracts,

4. there were differences between internal auditors in what was considered to be acceptable documentation and what was considered to be the definition of a unit of service, and

5. Internal Audit did not consider the risks evidenced by prior questioned costs at subrecipients when selecting which subrecipients would be reviewed.

Our analysis showed that from April 2005 to April 2007, the division's internal auditors completed 319 monitoring reviews from 501 active contracts. We reviewed 14 of the 319 monitoring reviews. Our review found that Internal Audit relied primarily on Daily Notes to determine whether contracted services were provided. The intended use of the Daily Notes was to document the clients' health and behavioral conditions, the descriptions of the services being provided, and the outcomes from such activities. The Daily Notes were prepared by individuals responsible for providing the services without any independent verification. Furthermore, the Daily Notes sometimes did not include information on the duration of the services being provided. This information is essential in determining the numbers of units of service provided. Since the Daily Notes were not independently verified, employees sometimes documented the estimated or scheduled times in and times out, instead of the actual times.

A better source of evidence would be the Visitor Sign In/Out Logs and service providers' employees' time sheets. The Visitor Sign In/Out Logs are maintained at the clients' residences and are regularly reviewed by the residential staffs. Employees' time sheets are reviewed through an internal control process within the providers' entities. Not examining the most reliable sources of evidence could result in the failure to detect overbillings by service providers.

In our review of the monitoring work performed by the division's internal auditors, we also noted that they selected their sample items from the Agency Payment Report, a billing summary, which did not include adjustments. However, the providers frequently made adjustments to the original billings, which were reflected on CS Tracking, the division's claims payment system, but the internal audit procedures did not include a review of adjustments. Our review of 1,113 charges for services from the 14 monitoring reviews revealed that 30 (3%) were later adjusted. Therefore, the numbers of units for these 30 charges for services tested by the division's internal auditors were not the numbers of units that the division ultimately paid. The internal auditors' failure to review adjustments decreased the division's ability to detect inaccurate and/or fraudulent billings.

We also found in our review that the internal auditors did not compare the total of Day Services (community-based, facility-based, and employment support day services) billed and paid to the maximum total units allowed. As a result, the division's internal auditors would not be able to discover excessive units of Day Services that might be billed.

Our review of the internal auditors' working papers revealed a lack of consistency among internal auditors concerning what was considered the minimum number of hours required in order to count as one unit of Day Services as well as what was considered acceptable documentation to support those services. As a result, different conclusions might have been made on the same item if it had been reviewed by two different internal auditors.

Furthermore, our review found that the planning of the monitoring effort was not comprehensive. The internal auditors did not analyze previously found questioned costs among various providers in selecting contracts to be reviewed.

Provider Manual

Our review also found that the Provider Manual governing contract performance was ambivalent on key aspects such as what constituted a unit of a given service and what was considered acceptable support for a service. The ambiguity of the Provider Manual made efficient and consistent contract management more difficult and increased the opportunities for inaccurate or fraudulent billings.

Providers were instructed to follow the guidelines and instructions in the Provider Manual when conducting business with DMRS. The Provider Manual, however, did not adequately define what constituted a unit of a given service and what was considered acceptable support for a service. Our inquiries with providers and the division's staff yielded various interpretations of what was required from the providers. For example, in regard to Day Services, Chapter 10 of the Provider Manual states:

> Day Services may be provided in settings such as specialized facilities licensed to provide Day Services, community centers or other community sites or job sites. Services may also be provided in the enrollee's place of residence if there is a health, behavioral or other medical reason or if the enrollee has chosen retirement. . . . Day Services shall be limited to a maximum of 6 hours per day.

Because Day Services were billed per day, the lack of a required minimum number of hours in order for a service to qualify as a unit provided the opportunity for providers to manipulate their billings. In addition, the Provider Manual did not require documentation for instances when services were provided at the enrollee's place of residence instead of at the designated facilities mentioned above. Due to the lack of other evidence or eyewitnesses to confirm services provided in residences, it is important that such information be clearly documented in some form, such as the Daily Notes.

Some amendments were made to the state's Medicaid waivers in July 2006, and the Office of Special Services prepared a summary document to give the vendors a reference guide of the changes. This document, titled "Changes for both State and Waiver funded services beginning July 1, 2006," states,

> The DAY service per diem for Facility Based on [or] Community Based may be billed if at least 2 hours of services were provided **WHEN** there is documentation that the person was unable to complete the full 6 hours for reason beyond the control of the provider.

Although the document indicated that meetings were held in each region in August 2006 to discuss the changes, our conversations with vendor management from Sunrise, Independent Opportunity, Omni Vision, and Pacesetters conducted in June 2007 revealed that only Pacesetters was aware of and followed the new guidelines. The other three providers stated that they billed DMRS if at least three hours of service were provided, with or without documentation for not providing the full six hours. The providers' widespread misunderstandings of the division's policies may have led to inaccurate billings.

Corrective Action for Subrecipients

We also found that DMRS had not considered the severity of questioned costs found among providers when determining the department's actions against subrecipients with questioned costs. In general, service providers with greater amounts of questioned costs and/or more instances of noncompliance should be subject to more severe disciplinary actions.

Each state agency is responsible for establishing and maintaining internal control to ensure effective management of all of its contracts. The division did take steps to provide monitoring by internal auditors and the auditors monitored quite a few vendors. But, as indicated by the issues disclosed in this finding, monitoring over service contracts was somewhat ineffective, which could result in payments for services not received. Guidelines and instructions on providing, documenting, and billing for services were inadequate and/or too ambiguous and not widely understood by the providers and employees, which could create opportunity for inaccurate and possibly fraudulent billings.

Recommendation

The Deputy Commissioner should review and discuss with the division's internal auditors ways to improve the effectiveness of the monitoring process in detecting inaccurate and fraudulent billings. The Director of Internal Audit should consider assessing the risk associated with each contract based on previous findings taking into account both quantitative and qualitative factors. The Director of Internal Audit should require internal auditors to also look at billing adjustments that are reflected on CS Tracking. The Director of Internal Audit should also compare the percentages of questioned costs amounts by providers and provide this information to the Deputy Commissioner, who should design appropriate disciplinary actions for providers with high percentages. The Commissioner should ensure that guidelines and instructions on providing, documenting, and billing for services are clear, specific, and widely understood by relevant employees and providers.

Management's Comment

Management does not concur. While indeed any audit or monitoring effort can always be improved, including the efforts of the Comptroller's Office, it does not warrant a finding.

Management does not concur with the auditors' comments on the DMRS Provider Manual. When changes to the provider manual because of waiver amendments and ensuing changes in service requirements occur between published versions of the DMRS Provider Manual, these changes are clearly communicated to division staff and the provider community in writing. Staff and providers are also forwarded written copies of any issues, terms, or conditions in the Provider Manual that DMRS management seeks to clarify. DMRS staff are currently updating the Provider Manual to incorporate all the waiver changes, service definition changes, and clarifying information that has been issued by the DMRS in the period since the current Provider Manual was issued. When completed, appropriate training sessions will be offered to providers.

Management always welcomes suggestions on how to improve already well-functioning processes such as those of its audit and monitoring unit and offer the following as evidence of such, some of which were also suggested by state auditors.

- Effective January 2007, meetings are held at least quarterly with appropriate staff. Standing goals include improving consistency between monitors, acquisition of skills and access to information to improve effectiveness and accuracy, and timely implementation of recent/needed changes.

- Effective January 2007, the DMRS reporting format was modified to address status of prior findings. This resulted in several "late" recoupments being finalized and the return of funds to both state and federal systems.

- Effective January 2007, quantitative and qualitative factors are taken into account. As shared with the state auditor in-charge in a follow-up interview after field work was completed, "Additional steps taken when deemed necessary and after consulting with the Internal Audit Director include:

    - Expansion of the sample to additional recipients and/or months

    - Verification of services rendered through the use of 3rd party verification."

- Effective January 2007, billing adjustments are factored in before final recoupment figures are communicated to the provider. DMRS will evaluate the practicality of incorporating this step at the "front end" of the monitoring process.

- The DMRS follows a calendar year monitoring cycle and audit staff are preparing a 2007 year-end summary report. The report will be provided to the Deputy Commissioner for his review and determination of additional follow-up work to be done. A sanction process is already in place for instances when disciplinary action is deemed appropriate.

Auditor's Rebuttal

Management stated that it did not concur with the finding and recommendations. Notwithstanding that statement, management did state that it was implementing, or considering implementing, all recommendations with the exception of the one pertaining to the Provider Manual.

Despite management's statements that necessary changes and clarifications to the Provider Manual are "clearly communicated" to staff and providers, our inquiries of providers and the division's staff yielded different interpretations of what was required from the providers. Clearly, management's attempts at communication have been ineffective.

2. The Division of Mental Retardation Services still had inadequate controls over the contract with the Community Services Network of West Tennessee, hampering the division's ability to properly administer the contract

Finding

As noted in the prior two audits, controls over the contract between the Division of Mental Retardation Services and the Community Services Network of West Tennessee, Inc. (CSN) were inadequate. Management concurred with the prior findings and in response to the most recent finding stated that they had done the following:

- Required CSN to sign a valid provider agreement as of July 1, 2005 and to submit claims through CS Tracking. These claims are eligible for federal financial participation and are being collected on a routine basis from TennCare.

- DMRS monitors are conducting annual reviews of CSN (beginning with calendar year 2005) to ensure that the state is receiving the services for which it is paying and to ensure that administrative costs are reasonable and necessary.

- The DPA for HCBS has been changed to include all services that CSN is authorized to provide.

Management's response to this finding from the earlier audit is exhibited in the appendix titled "Management's Comments From Prior Audits."

As of July 2007, the division had conducted a monitoring review of CSN to ensure that services were actually received and that administrative costs were reasonable and necessary. The division also had obtained an approved provider agreement, submitted eligible waiver services to TennCare for federal reimbursement, and modified the relevant Delegated Purchase Authority to include all Home and Community-Based Services provided by CSN. However, the division again failed to follow the contract provisions and still had not resolved a potential conflict of interest pertaining to a CSN board member. The division also failed to reconcile claims payments maintained by CSN to the amounts withdrawn from the division's account.

CSN was incorporated in March 2000, under the direction of a federal court monitor and with the assistance of outside consultants. CSN began operations in September 2000, after the federal court approved the CSN grant contract with the State of Tennessee. CSN coordinates and pays for health and behavioral services for and support of the Arlington class members living in the community who choose to become clients of CSN. According to its mission statement, "CSN is dedicated to improving the quality of life for individuals with developmental disabilities living in the community, through the coordination of medical, health and behavioral services and supports." For the period reviewed, July 2005 through December 2006, there were approximately 207 class members that received services through CSN. Total payments to CSN on behalf of these members for the same period totaled approximately $10,488,338. This averaged $50,668 per class member for that 18-month period, or $2,815 per month.

<u>Payment Methodology not in Accordance With Contract</u>

The original contract included three payment provisions, one of which was that the division would pay CSN $603.50 per month for each class member who was eligible to receive and did receive certain defined services and $803.50 per month for each additional class member over 200. However, in calendar year 2000, the division began paying CSN for actual expenditures related to class members, which were significantly higher than the contract amount. The amendments to the contracts that extended the terms through June 30, 2007, kept the same payment methodology wording, even though the division was paying actual costs. As mentioned above, the actual amount paid per month for the defined services averaged $2,815 per class member, or 361% more than the amount allowed under the contract.

As stated in the prior audit finding, to ensure timely payments to CSN for actual costs, the Division of Mental Retardation Services established a zero-balance bank account to reimburse CSN for its expenditures. This method of payment was contradictory to the portion of the contract that states, "the Grantee agrees to provide the State with monthly invoices, with all of the necessary supporting documentation, in a form acceptable to the State, prior to any reimbursement of allowable costs." This allowed CSN to automatically be reimbursed from state funds as checks written from CSN's account cleared the bank. No changes were made to this process during the audit period. Therefore, the division was still not reviewing support for the expenditures before they were paid.

Conflict of Interest

Furthermore, as reported in the prior audit and in CSN's independent auditor's report for the years ended June 30, 2005, and June 30, 2006, an officer of CSN who was a member of CSN's executive committee was also CSN's legal counsel. This individual also had a potential conflict of interest as a member of a law firm that provided legal counsel to a member of CSN's provider network. This could raise questions about transactions between CSN, on behalf of the Division of Mental Retardation Services, and the provider. CSN's independent auditor's report disclosed that payments to the mentioned firm for legal services for the years ended June 30, 2005, and June 30, 2006, totaled $56,373 and $57,076, respectively.

Payments not Reconciled

On a monthly basis, CSN submitted to the state a summary of administrative expenditures and an electronic data file of all medical claims paid during the month. The division, however, did not reconcile claims payment files to the amounts withdrawn from the division's account. Our review of CSN's medical payment files showed that CSN paid approximately $7.32 million for medical services in the period July 2005 to June 2006, but only about $7.16 million was withdrawn from the zero-balance bank account according to the State of Tennessee Accounting and Reporting System (STARS), resulting in an unresolved difference of $160,000 (2%).

Failure to correct these problems after they have been noted in multiple audits calls into question the control environment. By failing to enforce the provisions of the contract, top management is not setting the proper tone at the top, and the division may encourage other noncompliant practices. In addition, the continuing potential conflict of interest could give the appearance that certain arrangements may not be in the best interest of the state. Failing to reconcile CSN's claims payment records to the division's payment records undermines the division's ability to detect and prevent inaccurate and fraudulent transactions.

Recommendation

The Deputy Commissioner should take immediate steps to either amend the contract with CSN to reflect reality or rigorously enforce the provisions of the existing contract. The zero-balance bank account arrangement should be reviewed, and any other such arrangements should be reassessed and approved by the Commissioner. The Deputy Commissioner should ensure that all potential conflicts of interest are eliminated. The Commissioner should determine why the division does not reconcile payments for health and behavioral services to CSN's claims records.

Management should ensure that risks such as these noted in this finding are adequately identified and assessed in their documented risk assessment activities. Management should identify specific staff to be responsible for the design and implementation of internal controls to prevent and detect exceptions timely. Management should also identify staff to be responsible for ongoing monitoring for compliance with all requirements and taking prompt action should exceptions occur.

Management's Comment

Management concurs that there is still work to do to adequately control the CSN contract. DMRS management is currently in detailed discussions with CSN to determine why CSN has not completed all the necessary steps to become licensed as a Managed Care Organization (MCO) so they may be eligible for medical payments directly from TennCare as DMRS has requested in previous years. Absent a willingness of CSN to proceed with this recommendation, the DMRS will begin exploring less costly, more efficient alternatives to the current contract.

DMRS management will amend the payment terms in the fiscal year 2009 contract with CSN to reflect that actual costs are to be reimbursed to CSN for medial payments made on behalf of Arlington Class Members for which CSN is responsible.

DMRS management has requested detailed information to support CSN's draws from the zero-balance account effective with the January 2008 billing and CSN has agreed to supply such. This information will be reconciled monthly to CSN's payments as reflected in STARS.

The DMRS Deputy Commissioner will send a letter to the CSN Board member who appears to have a conflict of interest to tell him to remove himself from the Board. DMRS' Chief Counsel will review the apparent conflict of this member's firm working both for CSN and a CSN provider and make recommendations to the Deputy Commissioner. The Deputy Commissioner will then issue a written notice of corrective action needed to the CSN Board.

3. The Division of Mental Retardation Sevices has still failed to collect available federal reimbursement for waiver services, thus costing state taxpayers millions of dollars

Finding

As noted in the prior two audits, the process for obtaining reimbursement from TennCare for the Home and Community-Based Services (HCBS) waiver and Arlington/West waiver was inadequate, resulting in denied and pended claims that cost the state's taxpayers millions of dollars. Management concurred with the prior findings and in response to the most recent finding, stated:

> The DMRS [Division of Mental Retardation Services] now requests reimbursement monthly from TennCare through a HIPAA-compliant automated system. Amounts submitted to TennCare from CS Tracking are reconciled to STARS. Also, the DMRS established a group in March 2005 to reconcile, correct, and resubmit HCBS claims denied by TennCare. The efforts of this group have resulted in an increased number of successfully processed claims. The DMRS is now able to determine which claims have been paid, which have been denied, and which are in a pending file, enabling staff to reconcile amounts submitted to amounts reimbursed.

Management’s response to this finding from the earlier audit is exhibited in the appendix titled “Management’s Comments From Prior Audits.”

Claims Processing Still Ineffective

Although DMRS had implemented the mentioned corrective actions, the process was ineffective and inadequate in reducing the loss of federal revenue. Our review of the process for requesting and reconciling waiver services reimbursements from TennCare showed multiple weaknesses. As of May 15, 2007, the division had accumulated $23,000,000 of denied or pended claims for fiscal year 2006 waiver services paid in the period September 2005 to August 2006. The division had also accumulated another $8,000,000 of denied or pended claims for the first quarter of fiscal year 2007 waiver services paid in the period September 2006 to November 2006. DMRS has 12 months from the service date to submit a claim. If a claim is submitted within the 12-month period but the claim is rejected and the 12-month period has expired, DMRS gets a six-month extension to try and resolve the cause for rejection. After the claim is submitted again, DMRS has another six months. If problems with the claim have not been resolved within 24 months, DMRS would not receive reimbursement. Without taking immediate corrective actions, the division is likely to lose federal financial participation revenue for these eligible waiver services, when the period of availability of federal funds for the reimbursements ends.

In addition, due to the ineffectiveness of the reimbursement process in place during the audit period, DMRS did not receive reimbursement for all valid claims submitted. The division created a computer file of claims maintained on CS Tracking to be reimbursed from TennCare. This file was sent to TennCare, where it was entered into the TennCare Management Information System (TCMIS). TCMIS performed a data match, and one of three results occurred: (1) the claim was approved and paid; (2) the claim was denied; or (3) the claim was placed into a pended status within the TennCare system. The division received a report from TennCare detailing the number of claims paid and denied. However, the claims that were placed into a pended status were not reported to the division. Such claims were either approved or denied at a later time. The division then reconciled the amounts submitted to the amounts reimbursed. Doing so allowed the division to determine which claims had been paid, which had been denied, and which were in a pending file, thus enabling the division to correct and resubmit pended and denied claims. Our review of the division’s reconciliation schedule showed that as of May 15, 2007, the division had billed TennCare $446,038,183 for fiscal year 2006 waiver services but had only received $422,578,378 in reimbursements for these services, a shortfall of $23,459,805. Given that it has been more than 12 months since fiscal year 2006 ended and that the normal allowable period of submission is 12 months, it is very likely that most of the $23,459,805 shortage will never be collected. A similar review showed that the division also incurred a shortfall of $8,276,748 for waiver services provided in the first quarter of fiscal year 2007.

As noted above, the division’s effort to correct and resubmit denied and pended claims for reimbursement was ineffective and inadequate. The unpaid claims might be valid waiver expenses that were mistakenly rejected for being duplicates. When a client moved from one provider to another in the middle of the month, more than one payment might be made on behalf of the client for that month. TCMIS only allowed one claim for a given service per client per month and rejected the other claim as a duplicate. The division did not know how to fix these claims so they would be accepted by TCMIS. The division, instead, kept on resubmitting these claims, without making any correction, in order to extend its allowable period of submission. In addition, our review discovered a data-entry error in which two different clients had the same social security number on CS Tracking. Since TCMIS identified clients based on their unique social security numbers, claims for services provided to these two clients were also rejected as duplicates. Another explanation for large numbers of claims being denied or unpaid was that the division failed to ensure that clients receiving waiver services were actually eligible. In order to receive reimbursement for costs incurred in relation to waiver services, the division must ensure that the expenses were for financially and medically eligible recipients. The division contracted with the state's Department of Human Services for the services of determining and recertifying the financial eligibility of recipients for Medicaid coverage. The division also contracted with various Qualified Mental Retardation Professionals for the services of determining and re-evaluating the medical eligibility of recipients for Medicaid coverage. The determination and recertification of the financial and medical eligibility must be performed and filed with TennCare in order for the clients to be eligible for Medicaid coverage. In our testwork on clients who received waiver services in the tested months, we found 3 of 53 instances (6%) in which waiver services were provided to an ineligible client. The amount of waiver services provided was $35,652, which was 6% of the sample tested. Furthermore, the division's staff responsible for correcting and resubmitting denied claims stated that the volume of claims denied was such that the division had difficulty reviewing and resubmitting the denied claims in a timely manner.

During the audit period, the division requested and received approval to write off $66.6 million of receivables relating to waiver services from fiscal years 1997 to 2005, and the related administrative fees that were deemed ineligible for reimbursement. In the memo requesting the write-off, the Deputy Commissioner stated:

> The $66.6 million total results from a variety of factors including amounts recorded in the receivable that were ultimately determined to be non eligible for federal reimbursement, amounts for claims that did not meet the Center for Medicare and Medicaid Services' timely filing criteria, amounts to cover understatement of denied claims estimates for prior years, and amounts associated with individuals who were not eligible for the waiver program.

Despite the division's acknowledgement of the causes for its failure to optimize federal financial participation revenue, the division had not put in place corrective measures to effectively prevent the continuing loss of federal revenue.

TennCare not Billed for Adjustments

Corrections to previously billed services were entered into CS Tracking in the form of adjustments. Management stated that the division was not able to send adjustments to TennCare due to technical limitations. As a result, the division might have overbilled or underbilled TennCare. Our analysis of waiver services for fiscal year 2006 and the first quarter of fiscal year 2007 (corresponding to the payment period September 2005 to November 2006) showed that the division did not bill TennCare for $968,850 of eligible waiver services made through adjustments.

Because DMRS does not have an efficient and effective process for obtaining reimbursement from TennCare for waiver services, costs incurred through regular billings are often denied or placed in pended status awaiting corrections that don't get made in time to receive federal reimbursement, and costs incurred through claims adjustments are routinely not reimbursed. This deficiency costs the state's taxpayers millions of dollars per year.

Recommendation

The Assistant Commissioner of Administration should hold a discussion with TennCare and the division's IT staff to find a solution to the problem of denied claims being mistakenly rejected by TennCare. The division's Director of Information Technology should seek the design of a computer program to identify clients receiving waiver services that are not eligible. The program should match CS Tracking's payment data files to TennCare's eligibility data files prior to paying the provider. The Assistant Commissioner of Administration should impose appropriate disciplinary actions on responsible parties for their failure to obtain Medicaid coverage for clients. The Assistant Commissioner of Administration should closely review the payment and reimbursement cycle, identify any other deficiency leading to the loss of federal financial participation, and find a way to correct these deficiencies. The Commissioner should closely monitor and evaluate the progress and efficiency of the resubmission of denied claims for reimbursement and should ensure that division staff fulfill that responsibility and are held accountable for their shortcomings. The Assistant Commissioner of Administration should hold a discussion with TennCare and the division's IT staff to find a solution to allow the division to submit and receive reimbursements for adjustments to previously billed services.

Management's Comment

Management asserts that the lead sentence in this finding presents an unbalanced picture to readers of this audit. While management concurs that the reimbursement process in place during the time period of this audit had inadequacies, management has addressed these issues and is successfully collecting federal reimbursement for waiver services and administrative costs at 99.5% of expenditures on the first filing with TennCare, since May 2007.

To ensure that federal dollars are being received when earned, the DMRS instituted a new payment methodology in July 2007. The new methodology addressed the auditors' concerns in this and prior audits. The new process reverses the payment process. DMRS now electronically submits providers' billings to TennCare but does not reimburse the providers until payment is received from TennCare. DMRS then pays the provider only the amount of the TennCare reimbursement. This additional edit process gives early identification of eligibility issues and prohibits automatic payment. In some cases TennCare reimbursement is not forthcoming for part of a provider's billing due to no failure on the part of the provider. DMRS may make the decision to reimburse the provider and then actively pursue reimbursement from TennCare.

The new unit created to audit denied claims was going through a very steep learning curve during the period covered by the audit and did not have adequate time or resources to clean up years of denied claims before the auditors left the field. As of January 2008, the DMRS' process for working denied claims looks very different. Denied and suspended claims are quickly identified and routed to DMRS field staff for immediate action. The Denied Claims Unit is working closely with Tenncare, DHS, and DMRS Information Technology to identify and correct errors expeditiously. DMRS has worked closely with DHS to correct old eligibility issues, and most all of these have been resolved. The close relationship with these agencies also allows for early detection of new issues such as new edits being used by Tenncare.

Also, necessary updates to the existing system made for the payment reversal process has improved the timeliness and accuracy of the resubmitted claims. DMRS management also notes that some issues are exacerbated by problems with the TennCare Management Information System. For example, while a DMRS service recipient may have two different providers performing the same service within a one-month period (one vendor the first half of the month and another vendor the second half of the month) which produces a valid claim on the part of both vendors, the TennCare system cannot distinguish a partial month period and thus will deny the claim that it receives last in this particular scenario. DMRS continues to work diligently with TennCare to identify and correct issues such as this.

Auditor's Comment

We disagree with management's statement that "the lead sentence in this finding presents an unbalanced picture to the readers of this audit." We believe the information we have presented is indeed factual. The finding addresses the problems noted during our audit period. As noted by management in their comment, the corrective actions were not instituted until after our audit period.

4. <u>The Division of Mental Retardation Services has again arbitrarily paid for housing subsidies without rules for eligibility</u>

Finding

The Division of Mental Retardation Services (DMRS) pays providers for many types of services for its eligible clients. One of the payment types made to these providers is referred to as housing subsidies. These subsidies are to help supplement room and board costs (i.e., rent or mortgage payments, food, etc.). This is a fully state-funded subsidy and is provided in addition to what the provider may be receiving for the clients' needs from social security. The division pays the subsidy to the direct service provider, who subsequently pays for the mortgage or rent of the client. As noted in the prior audit, the division had no written policies or procedures to provide this subsidy equitably to all eligible clients. Management concurred with the prior finding and stated:

> The DMRS continues to work toward a viable set of rules for housing subsidies that takes into account the very limited income of most persons with mental retardation, the limited funding available for housing subsidies, equality of access to funding for subsidies, the expectations of the parties in the lawsuits, the availability of housing stock suitable for people with special needs, and agreed upon reasonable and necessary costs for room and board.

Since the last audit, the division drafted the mentioned policies and procedures; however, the draft had not been approved and implemented as of July 2007. In addition, the drafted policies and procedures lacked specificity on several key elements, thus hampering the division's ability to guarantee equitable treatment to all eligible clients as defined in the draft. Furthermore, the preferential treatment reserved for eligible clients might lead to additional lawsuits filed on behalf of clients, not deemed eligible, who want to receive the same treatment. As also noted in the prior audit, there were no written policies or procedures to regulate the total state funds spent to provide this supplement, and the division still paid rents that appeared much higher than those estimated by the U.S. Department of Housing and Urban Development on several properties.

The prior audit noted that there are no federal or state requirements for the state to provide this supplement and that MR Housing was added as a solution to satisfy lawsuits the division had been involved in over several years. However, management never provided any documentation where the courts specifically ordered this subsidy or explained who would be required to receive the subsidy.

The Director of Special Services stated that when a client requested the housing subsidy, an employee performed a calculation that determined the client's need for assistance based on budgeted costs and incomes submitted from the regional office and the client's provider. The draft of the Housing Cost Subsidy Policy, Part D. 6, states:

> The determination of the amount of a Housing Costs Subsidy shall be at the sole discretion of DMRS and shall be based on an assessment of the service recipient's income (both earned and unearned) and reasonable residential costs.

However, we noted that the calculation was not consistently followed throughout the division and was not consistently applied to all eligible clients. In addition, there were no established guidelines on what were considered reasonable residential costs. The Director of Special Services confirmed that if there were two or more individuals with similar income and similar medical needs that requested the subsidy, one might receive the housing supplement and one might not. She also confirmed that the clients who were class members of the lawsuits received priority. In our review of a sample of 34 calculations of housing subsidies, we noted that three (9%) were either incorrectly computed or the results of the calculations were not properly followed.

Our analysis of housing subsidy payments made for January 2007 showed that 802 clients received housing subsidies. Some clients lived with one or more other clients, but 458 of these clients lived in a dwelling by themselves at greater expense to the state.

DMRS management explained that they had decided that clients could be approved for the housing subsidy when their expenses exceeded their ability to pay for their living expenses. Property was either purchased by the client or rented by the client. Also, any necessary modifications to the property to accommodate the client’s needs (i.e., wheel chair ramps, roll-in showers, widened doorways) were paid for by DMRS. Once the modifications were completed and the client had moved into the housing, it was subsequently difficult and/or expensive to move the client into other housing not having the modifications. Therefore, when a property was rented, the landlord could raise the rent without the fear of DMRS moving the client into other housing. Eventually the state could be paying rent at above-market rates for many years, and the client and/or the state would have no asset. Based on review of the amounts paid, housing subsidies (including rent, mortgages, food, utilities, and household and personal maintenance, net of the clients’ incomes) of over $900 per month were provided to help pay for rent or mortgages on behalf of 55 residents, which totaled $529,027 for the period February 1, 2005, through January 31, 2007.

Based on our review of January 2007 housing subsidies for single-occupant homes of $900 or more, DMRS paid $900 or more specifically for rent or mortgages on behalf of 19 residents out of 21 reviewed (90%). Some of these properties were reviewed, and the cost and appraised values were obtained. Based on these 21 cases, the average rent for January 2007 was $1,054, and the average 2006 appraised value of these homes was $106,195 (or about 101 times the January rent). In seven cases, these properties’ appraised values were less than 90 times their January 2007 rent. January 2007 rent payments for these seven cases were $950, $1,000, $1,000, $1,074, $1,200, $1,330, and $1,330 for homes with appraised values of $65,300, $81,400, $85,000, $85,100, $100,500, $95,200, and $95,800, respectively. The highest housing subsidy paid for any one client in January 2007 was $1,587, which included $1,100 for rent of a house owned by the client’s father.

Our review of January 2007 housing subsidies for clients who lived in two-occupant homes indicated that the average rent for January 2007 was $1,515, and the average 2006 appraised value of these homes was $123,120 (or about 81 times the January rent). Of the five properties reviewed, two (40%) were appraised at less than 80 times their January 2007 rent. January 2007 rent payments for these two cases were $2,112 and $1,294 for homes with appraised values of $123,700 and $98,800, respectively. On May 21, 2007, DMRS received approval from the State Building Commission to purchase the property that had the January 2007 rent of $2,112. The Assistant Commissioner of Administration stated that the division had obtained all necessary approvals and funding for the purchase but had not finalized the purchase as of July 24, 2007.

Our review of January 2007 housing subsidies for clients who lived in three-occupant homes revealed that January 2007 rent for one of the shared units totaled $3,000. This property’s 2006 tax appraisal value was $121,700. As mentioned in the prior audit, this property was purchased by Hearthwood Properties, LLC, and leased to the state for $3,000 per month for ten years. This special arrangement was entered into with the lessor to buy certain specially equipped properties that DMRS determined were necessary for its clients at rates above fair-market value. The lessor also had to make some additional modifications to the property, resulting in an inflated monthly lease. On May 21, 2007, DMRS received approval from the State Building Commission to purchase this property. This purchase had not been finalized as of July 14, 2007.

Rents paid for the properties discussed above were much higher than those estimated by the Policy Development and Research Information Services of the U.S. Department of Housing and Urban Development (HUD) as published in its annual Fair Market Rents studies. For example, the Final (Federal) Fiscal Year 2006 Fair Market Rent estimated that rents in Shelby County Tennessee were $572, $636, and $847 per month for a one-bedroom unit, two-bedroom unit, and three-bedroom unit, respectively.

Furthermore, we obtained a list of all DMRS housing payments made from April 1, 2005, through March 31, 2007, which were for the period February 28, 2005, through January 31, 2007, summarized by service period. Similar to the prior audit, seven instances were noted when two DMRS housing payments were paid on behalf of a single individual for a single month due to duplicate payments or erroneous adjustments, resulting in a net overpayment of $1,515.

If the division continues to provide this service without standardized policies and procedures, additional legal matters could arise or, as more and more residents request the supplement or the rents increase on the units already being utilized, costs will continue to escalate.

Recommendation

The Deputy Commissioner should review the division's current processes related to this service and complete and implement policies and procedures that address the division's position on these issues. The Deputy Commissioner should review and revise the drafted policies and procedures to ensure that they are adequately descriptive in order to provide equitable treatment for all clients. These policies and procedures should address situations in which rental property is involved to ensure that the state pays a fair value and to set a limit on the amount of rent a client could include in his/her budget, which would be used to calculate his or her subsidy. Similarly, the policies and procedures should ensure that subsidized mortgage payments are limited to a reasonable amount. The Deputy Commissioner should expedite the purchases of approved properties that are currently under long-term lease arrangements. The Deputy Commissioner should perform buying vs. renting analyses for existing subsidies in which rental properties are involved. The division should establish an effective mechanism to prevent, detect, and recover overpayments.

Management should ensure that risks such as these noted in this finding are adequately identified and assessed in their documented risk assessment activities. Management should identify specific staff to be responsible for the design and implementation of internal controls to prevent and detect exceptions timely. Management should also identify staff to be responsible for ongoing monitoring for compliance with all requirements and taking prompt action should exceptions occur.

Management's Comment

Management concurs that it did not have an approved housing subsidy process in place during the audit period. Management now has an approved housing subsidy process that includes defined methodology for determination of subsidy amounts. In addition, new subsidies are only approved for class members. Subsidies issued prior to this policy were not canceled, but the DMRS is looking at ways to control costs of these subsidies, such as purchasing properties where the monthly lease amount appears to be higher than that particular market's average rate.

Management does not concur with the state auditors' analysis tying reasonable lease rates to appraised values of property. While certainly that is a factor to consider, average lease rates vary widely from community to community based on such factors as availability of competing properties, willingness of owners to allow modifications to be made that are required by DMRS service recipients, and the general economic conditions of the community in which the property is located.

Finally, it is unclear to management what the auditors are recommending concerning individuals already receiving a subsidy that was not calculated using the approved policy in place.

Auditor's Rebuttal

We did not intend to imply that the appraised value of a property was the only factor to consider in determining the reasonableness of a lease rate, but it is definitely something that should be considered along with other factors that management deems relevant. Also, we would expect management to review any existing subsidies on a case-by-case basis for compliance with the approved policy.

5. <u>The Division of Mental Retardation Services has still failed to strengthen controls over the payment process and its claim system, Community Services Tracking; thus, it overpaid providers hundreds of thousands of dollars and created a fertile ground for fraudulent transactions</u>

Finding

As noted in the prior audit, the security and internal controls over the Community Services Tracking System (CS Tracking) were inadequate. Management concurred with the prior finding and stated, "DMRS [Division of Mental Retardation Services] is addressing the general inadequacy of the CS tracking system by replacing it." However, as of the end of July 2007, the replacement of CS Tracking had not been completed. The IS Director stated that they will replace four of the functions in this system in January 2008, and it is the division's plan to replace the whole system in the future; however, she couldn't say when that would happen. The control weakness concerning data-entry mistakes in entering service invoices had been partially corrected. Regular billings are directly entered by providers through a web-based application instead of being entered manually by the division's employees, and the web-based application provides certain edit functions, which should reduce the number of errors. However, billing adjustments still have to be entered manually. In addition, our review discovered several other control deficiencies. The prevalence of security and control flaws over CS Tracking and the payment process led to overpayments or improper payments, as discussed below, of hundreds of thousands of dollars and continued to create numerous opportunities for fraudulent transactions.

Adjustments to previously billed invoices could not be entered through the online application which was developed for regular billings, so the adjustments were still entered manually. The adjustments typically were to correct errors in the number of units of service billed. In response to the prior audit, management stated, "DMRS Information Technology (IT) is currently working on an additional component for the Provider Claims Processing application that will enable providers to also bill their claim adjustments through the web application." However, as of the end of July 2007, the implementation of the web application for the billing of claim adjustments had not been completed. Our analysis revealed numerous instances of overpayments or improper payments resulting from poor control over payments processed through adjustments as detailed below.

A computer-assisted audit technique (CAAT) was performed on payment records for the service months of February 2005 through January 2007, which corresponded to the payment months of April 2005 through March 2007, maintained on CS Tracking. This CAAT identified all records of services that appeared to be billed and paid multiple times in the form of adjustments. Of the 706 possible overpayments identified, the division stated that 315 had been detected and corrected by the division after we obtained the payment data used in this analysis. Therefore, we selected a sample of 50 items from the items that management stated had been discovered and corrected, and compared them to the CS Tracking Payment Screen on July 10, 2007. Our testwork showed that 14 of the 50 items reviewed (28%) had not been corrected. These uncorrected overpayments amounted to $710, or 0.6%, of the sample of $119,810. The total amount of the population was $749,105. For two of the items, the amounts were paid twice, first on February 1, 2007, and then again on March 1, 2007, apparently due to a computer malfunction. For the other 12 items, the wrong rates had been used, and since adjustments are made manually, the normal cost plan controls were bypassed. In regard to the corrected errors, the division essentially loaned the providers hundreds of thousands of dollars for several months until the division identified and corrected these overpayments.

The remainder of the 706 possible overpayments included 312 charges that had multiple identical records and 79 charges that had multiple, but not identical, records. The multiple, but not identical, records were instances where there were multiple payments for the same client for the same month for the same service, but with different amounts. Our review of a sample of 28 of the 312 charges revealed 17 duplicates/overpayments (61%) and one underpayment (3%), for a net overpayment of $13,046, or 15%, of the sample of $86,312. The total amount of the population was $628,479. These errors could have resulted from any of the following: (1) one payment was made through regular billing, and one was through an adjustment; (2) both were made through adjustments, and the employee did not determine that the adjustment had already been entered; and (3) the client moved from one provider to another, and both providers billed for the same service.

Our review of a sample of 25 of the 79 charges that had multiple, but not identical, records revealed 11 duplicates/overpayments (44%) and 3 underpayments (12%) for a net overpayment of $8,435, or 8%, of the sample of $100,902. The total amount of the population was $313,605. These errors may have been due to the fact that the rate for each service changed frequently, and the system did not pick up the correct rate or the person entered the wrong rate.

Our analysis of adjustments to identify possible data-entry errors, stemming from a common keying mistake in which rates were entered as units, found two keying errors. In the first instance, the employee mistakenly entered 338 units at $338 per unit instead of 1 unit at $338 per unit. In the second instance, the employee not only mistakenly entered 300 units at $300 per unit instead of 1 unit at $300 per unit, but also did not know that the adjustment had already been made. The overpayments of $114,244 and $90,000 were made and deposited into the providers' accounts. The division subsequently did recover these two overpayments from the providers, who notified the division upon the providers' discovery of the overpayments. As noted in the prior audit and again in this audit, the division had not performed any reconciliation to ensure that the amount billed agreed to the amount paid. Such reconciliation would enable the division to proactively and systematically detect such data-entry errors.

Our review of CS Tracking revealed another system edit control deficiency that would allow providers to bill and get paid for more than the maximum total units of Day Services (community-based, facility-based, and employment support day services) allowed. Our testwork on a sample of 25 of 576 sets of Day Services whose total units exceeded the total units allowed showed that 19 (67%) had not been corrected as of July 10, 2007. Payments for units of Day Services above the maximum total units for these 19 cases amounted to $6,441, or 14%, of the sample of $47,168. The total amount of the population, net of those items that were included in other populations discussed above, was $1,119,421.

As noted in the prior audit, CS Tracking had serious control deficiencies concerning information security. In response to the prior audit, management concurred and identified corrective actions to mitigate or eliminate the risks associated with these deficiencies. However, based on our discussions with the Administrative Directors of the three regional offices and the Director of Special Services in Nashville during the current audit, we were told that 42 of 109 employees reviewed (39%) had higher levels of access than that required by their jobs. We found two instances where employees that had been terminated in 2006 still had access as of June 2007. One of these two employees had access to multiple critical functions that could be used to commit serious financial frauds. In addition, our review of the passwords of 750 users revealed that 320 (43%) violated the most basic and essential control over passwords, which we are refrained from disclosing in detail because disclosing those specific vulnerabilities could present a potential security risk by providing readers with information that might be confidential pursuant to Section 10-7-504(i), *Tennessee Code Annotated*. We did provide the department with detailed information regarding the specific vulnerabilities identified as well as recommendations for improvement.

Some employees who had the access capability which allowed them to enter payment information into the system also had the ability to make adjustments without any independent verification or approval. Adjustments bypassed controls related to cost plan limitations and allowed the user to enter any payment amount desired. A cost plan is a service plan that has been proposed and approved by mental retardation and service support professionals based on the individual's need for services and his or her level of need, and the amounts and types of services provided are supposed to be in accordance with the plan. Our review showed that eight employees had access that enabled them to initiate, edit, and approve payments and to make adjustments. As also noted in the prior audit, the application was capable of producing error reports; however, these reports were neither automatically generated nor required to be reviewed. The current Accounting Manager stated that monthly reports of adjustments are generated for each region, and an Account Tech is assigned to scan the reports for unusual entries, but this review is not documented.

In addition, DMRS still did not maintain adequate and updated documentation related to the application for users and programmers to follow. The application lacked the following documentation: (1) instructions for restarting the application and for backup and recovery, (2) comprehensive instructions for application users, (3) explanations of internally generated transactions and calculations, (4) flow charts and/or data flow diagrams, and (5) software security information.

A lack of appropriate security could lead to faulty or fraudulent data in CS Tracking and compromise clients' confidentiality. Without adequate segregation of duties, inappropriate additions or changes could be made without being discovered. The risk of fraud is significantly increased when computer controls are weak. Data entry reconciliations and automatic generation and review of error reports are necessary to reduce improper payments and overpayments. If the division does not maintain proper system documentation, users may unknowingly be performing functions improperly.

Recommendation

As the Division transitions from CS Tracking to the new claim system, the Deputy Commissioner should ensure that adequate security controls are established. Until the division is able to process billing adjustments through the online web-based application, the Deputy Commissioner should immediately put in place effective compensating controls to detect and prevent overpayments processed in the form of adjustments. Likewise, the Deputy Commissioner should implement controls to detect and prevent payments made for Day Services that exceed the maximum numbers of units allowed for given months. The Deputy Commissioner should immediately investigate overpayments discovered during our audit and take actions to recover these overpayments. Employee access to CS Tracking should be immediately reviewed and modified appropriately. The Deputy Commissioner should immediately review and identify control violations over passwords and take appropriate disciplinary actions on known violations. The Deputy Commissioner should also ensure that appropriate documentation related to the new claim system be maintained and kept up-to-date.

Management should ensure that risks such as these noted in this finding are adequately identified and assessed in their documented risk assessment activities. Management should identify specific staff to be responsible for the design and implementation of internal controls to prevent and detect exceptions timely. Management should also identify staff to be responsible for ongoing monitoring for compliance with all requirements and taking prompt action should exceptions occur.

Management's Comment

Management concurs that controls have not been strengthened in the community services tracking system. The Division has spent a great deal of time, effort, and resources on developing a detailed requirement plan to create and implement a new information system which will incorporate the types of controls the auditors have noted as necessary. The process has gone slower than anticipated, but DMRS management is committed to completing this project as quickly as possible without jeopardizing any elements of the system.

Management concurs that more caution should be exercised when making adjustments to CS Tracking to ensure that duplicate or erroneous amounts are not paid.

Management has reiterated to division managers the importance of notifying the appropriate individuals in DMRS central office to reduce or eliminate an employee's access to CS Tracking when the employee's job duties change or the employee leaves service with the Division.

DIVISION OF MENTAL RETARDATION SERVICES' CONFLICT-OF-INTEREST POLICY

The objective of our review of the Division of Mental Retardation Services' (DMRS) conflict-of-interest policy was to follow up on the prior-year finding regarding DMRS not following the established conflict-of-interest policy. We interviewed key personnel and reviewed nonstatistical samples of personnel files of employees hired from April 2005 to March 2007, to determine whether DMRS had an effective conflict-of-interest policy and whether the conflict-of-interest policy was followed. As a result of our work, we determined that the conflict-of-interest policy at the central office was adequate and in place; however, conflict-of-interest policies had not been fully implemented at the regional offices and the developmental centers, as discussed with management.

DIVISION OF MENTAL RETARDATION SERVICES' TRAVEL CLAIMS

The objective of our review of the Division of Mental Retardation Services' travel claims was to follow up on the prior-year special investigations finding regarding the Deputy

Commissioner's failure to monitor and review an administrator's work activities and travel claims submitted to him for reimbursement, enabling the administrator to overbill mileage. We interviewed key personnel and reviewed relevant documentation to gain an understanding and to evaluate the adequacy of the controls and procedures over employees' travel claims. We selected and tested a nonstatistical sample of employees' travel claims submitted for reimbursement to determine whether the controls over travel claims were in place. As a result of our work, we determined that controls over employees' travel claims were adequate and in place.

DIVISION OF MENTAL RETARDATION SERVICES' PERSONNEL PROCEDURES

The objectives of our review of the controls and procedures over the Division of Mental Retardation Services' personnel procedures were to determine whether

- proper documentation was kept in DMRS personnel files, and
- improper employer/employee relationships existed.

We researched the Department of Personnel's requirements and state law to determine which documents are required to be maintained in each employee's personnel file. We selected a nonstatistical sample of DMRS employees as of March 7, 2007, to ensure their personnel files contained the proper documentation. In addition, we reviewed the contracts tested as part of the contract management review and examined the supervisory structure at the developmental centers and regional offices to determine whether improper employer/employee relationships existed.

We determined that the division was complying with the Department of Personnel's requirements and state law regarding personnel files. As noted in finding 6, improper employer/employee relationships were identified.

6. The Division of Mental Retardation Services still had improper employer-employee relationships, raising serious policy and legal issues

Finding

As noted in the prior three audits, the West Tennessee Regional Office and the three developmental centers of the Division of Mental Retardation Services had established improper employer-employee relationships. Management concurred with the prior finding and stated, "DMRS [Division of Mental Retardation Services] will continue its concentrated effort to convert as many contracts as possible during calendar year 2006 and 2007." Management's responses to this finding from the earlier audits are exhibited in the appendix entitled "Management's Comments From Prior Audits." Since the last audit, the division had successfully reduced the number of contractors which either supervised state employees and/or were supervised by state employees by 55%, from 143 down to 65.

We obtained copies of all personnel contracts from the division's contract officer. Based on our review of the contracts and discussions with staff at the various locations, the following was noted:

Arlington Developmental Center in Memphis had 55 contractors, 8 of whom (15%) supervised state employees and/or were supervised by state employees. The West Tennessee Regional Office in Memphis had 33 contractors, 2 of whom (6%) were both supervised by state employees and supervised state employees. Clover Bottom Developmental Center in Nashville had 71 contractors, 45 of whom (63%) were supervised by state employees. Greene Valley Developmental Center had 17 contractors, 10 of whom (59%) were supervised by state employees.

Chapter 0620-3-3-.07 of the *Rules of the Department of Finance and Administration* requires that "State employees shall be hired through the merit system of the Department of Personnel." Section 8-30-201(a), *Tennessee Code Annotated*, establishes "a system of personnel administration based on merit principles and scientific methods. That system shall govern the appointment, promotion, transfer, layoff, removal and discipline of employees, and other incidents of state employment." Section 8-30-201(b), *Tennessee Code Annotated*, gives the Department of Human Resources, formerly the Department of Personnel, the responsibility of administering and improving this system. By entering into these contracts, the department in effect circumvented the state's employment process for obtaining staff.

Furthermore, the practice of allowing employees of non-state entities to report directly to department officials/employees in carrying out what could be construed as state programs raised serious policy and legal issues. The manner in which the contract employees were utilized by the division met multiple tests and criteria established by the IRS and upheld by Tennessee case law defining employee status. The division controlled the manner in which contractors performed services, the division established the working hours and workplace arrangements, the contractors performed services that supplement division staff, and the tenure of most contractors was continuing. All of these factors met the criteria that defined employee status.

Recommendation

Where employer-employee relationships exist, individuals should be placed on the state payroll system through the proper hiring procedures established by the Department of Human Resources. If the skills and duties needed do not exist in any state personnel classification, the Commissioner should continue to work with the Department of Human Resources to create a proper classification. If the Division of Mental Retardation Services is unable to fill vacant positions because of inadequate pay ranges, the Commissioner should again continue to work with the Department of Human Resources to obtain the necessary changes to the job classifications.

Managements' Comments

Department of Finance and Administration

Management concurs and will continue to work with the Department of Human Resources to create appropriate classifications at appropriate pay grades so as to convert the contractors in question to state positions. The Deputy Commissioner is preparing a letter to all program staff outlining what activities are not to be done with contractors, e.g., supervising state employees and what activities cannot be done by state employees regarding the contractors, e.g., supervising their fulfillment of their contractual obligations to the state. In addition, a copy of the IRS' indicators of employee versus contractor will be distributed to program supervisors.

Department of Human Resources

The Department of Human Resources agrees our agency should continue to work with the Division of Mental Retardation Services to address concerns related to classification and compensation. To that end, we have initiated a conversation with the Division of Mental Retardation Services to review both the classification and pay issues.

DEVELOPMENTAL CENTERS' OPERATIONS

Our objectives in reviewing the controls and procedures over the developmental centers' operations were to determine whether

- equipment records at Arlington Developmental Center were accurate;
- resident trust fund accounts were reconciled with bank records;
- disbursements from resident trust funds were in accordance with established policies and procedures; and
- petty cash accounts at the centers could be accounted for.

We interviewed key personnel at Arlington Developmental Center to obtain an understanding of their controls and procedures for equipment. We selected a nonstatistical sample of equipment as of February 23, 2007, to determine the accuracy of the information recorded in the Property of the State of Tennessee (POST) system. Based on the testwork performed, we determined that recordkeeping for equipment at Arlington Developmental Center was adequate.

We interviewed key personnel at each center to obtain an understanding of the controls and procedures for resident trust accounts. We randomly selected and reviewed a monthly reconciliation of the resident trust account with bank records for each developmental center to determine whether the reconciliation was properly performed and adequately supported. We selected nonstatistical samples of purchases made on behalf of the residents from the reviewed months to determine whether purchases were made in accordance with the centers' policies and procedures. Based on the testwork performed, we determined that for the months examined reconciliations were performed and were adequately supported. We also determined that trust fund policies and procedures were not always followed and controls over the resident trust accounts at Clover Bottom Developmental Center and Greene Valley Developmental Center were inadequate as noted in findings 7 and 8, respectively. At each center, we also interviewed key personnel to obtain an understanding of the controls and procedures over the petty cash account. We also performed a surprise cash count to determine whether the petty cash account's balance was in agreement with the balance on the center's records. Based on the testwork performed, we determined that the imprest balances of petty cash accounts were accounted for.

7. Internal control over resident trust funds at Clover Bottom Developmental Center was still inadequate, increasing the risk for misuse or loss

Finding

As noted in the prior audit, Clover Bottom Developmental Center (CBDC) had multiple internal control deficiencies related to the resident trust accounts and purchases from these accounts. Management concurred with the prior finding and has taken steps to correct some of the deficiencies; however, additional improvements are needed to mitigate the risk for misuse. Employees did not always follow established procedures for distributions of cash to residents and for purchases made on behalf of the residents. There was cash outstanding from the funds for excessive periods. Some purchased items could not be located and were not entered into the residents' inventory records. Total disbursements from the resident trust funds for the 26-month audit period were $974,849.

The purpose of these trust funds is to receive and disburse funds on behalf of the residents at CBDC. The residents' income is deposited and maintained in a state bank account designated for this purpose. The accounting records of this account are detailed to indicate the amount of money each resident has on a day-to-day basis. Residents receive money from various sources, such as the Social Security Administration, relatives, and jobs. CBDC has a fiduciary responsibility for maintaining accurate records and internal control over these funds.

CBDC's Policy A.9.2, effective March 17, 2006, states that employees who withdraw monies from the residents' accounts to make purchases on behalf of the residents must attach a sales slip, invoice, and/or cash register receipt to the Request for Funds and forward it to the Accounting Office within five working days of signing for the funds. Our review of 229 requests for funds made in January and February 2007 showed that 52 requests (23%) were not settled within five business days. These 52 requests were outstanding from 8 to 59 days and totaled $5,879 (20% of the population total of $29,882).

CBDC's Policy A.8.2 requires that when the designated purchaser returns with the items purchased, the sales slip and all items must be checked and verified immediately by a supervisory staff member who signs the sales slip indicating the verification has been made. Our review of 229 requests for funds made in January and February 2007 showed that 27 requests (12%) did not have the required signature from an independent employee at the resident's home.

CBDC's Policy A.9.1 requires that items purchased be recorded on the individual's inventory records immediately after purchases are made. Our review of 28 items purchased in January and February 2007 for the residents showed that four items (14%) were not recorded in the inventory records and they could not be physically located. For another item which could not be located, management asserted that the item had been moved with the resident to a new home in the community. However, the staff at the resident's new home stated that the item was not with the client when the client moved to the home.

In accordance with CBDC's policy, allowances earned by residents for doing chores are distributed to the residents by an accounting clerk in the presence of two witnesses who sign the disbursement forms indicating that the monies were given to the correct residents. The accounting clerk who distributed the cash kept the forms signed by the witnesses; however, no independent accounting staff reconciled the forms to the cash given to the accounting clerk to ensure it was actually distributed to the residents or returned to the account. The average amount of cash distributed to residents per month exceeded $2,400.

Without adequate internal control over the resident trust accounts, residents' funds could be lost or stolen. When the settlement of funds distributed to employees is delayed, the chances of loss, theft, or inappropriate use increase, and the residents may not be receiving the needed goods and services in a timely manner. Without an independent review of purchases, items may not be properly recorded in the individual's inventory. Furthermore, if the distribution of funds by the accounting clerk is not reviewed, funds could be stolen and mistakes could go unnoticed.

Recommendation

The risks identified in this finding should be immediately addressed. The security of residents' funds should become a priority for the Commissioner of the Department of Finance and Administration, the Deputy Commissioner for the Division of Mental Retardation Services, and the Superintendent of Clover Bottom Developmental Center. They should determine why the center's employees have been allowed to disregard policies established to safeguard residents' funds. They should assign specific staff the responsibility of ensuring that the established controls are followed, and someone should be assigned to follow up on the instances noted where residents' property was not properly accounted for and determine what happened. Appropriate disciplinary action should be taken when employees violate control policies.

The Deputy Commissioner should ensure that time limits for funds outstanding are enforced, that all employees follow established procedures for verifying trust fund purchases, and that all purchases are accounted for in the inventory. Independent accounting staff should reconcile the disbursement forms with the monies given to the accounting clerk for distribution.

The Deputy Commissioner should ensure that risks such as those noted in this finding are adequately identified and assessed in documented risk assessments at all developmental centers. The Deputy Commissioner should identify specific staff to be responsible for the design and implementation of internal controls to mitigate the risks identified. The Deputy Commissioner should also identify specific staff to be responsible for ongoing monitoring for compliance with all requirements and taking prompt action should exceptions occur.

Management's Comment

Management concurs and has rewritten its trust fund policy to strengthen controls indicated by the state auditors and to clarify employee responsibilities relating to cash. In addition, employees of CBDC will receive additional training on the importance of timely recording changes to recipients' inventory lists so that missing items will be recognized immediately and corrective action taken.

8. Controls over resident trust funds at Greene Valley Developmental Center were inadequate, increasing the risk for misuse or loss

Finding

Controls over resident trust funds at Greene Valley Developmental Center (GVDC) were inadequate. Employees did not return unspent residents' funds to the center's accounting department within the time frame required by policy and did not place funds in the safes at the homes when the funds were not being used to fill the residents' requests.

The purpose of these trust funds is to receive and disburse funds on behalf of the residents at GVDC. The residents' income is deposited and maintained in a state bank account designated for this purpose. The accounting records of this account are detailed to indicate the amount of money each resident has on a day-to-day basis. Residents receive money from various sources, such as the Social Security Administration, relatives, and jobs. GVDC is responsible for maintaining accurate records and internal control over these funds.

At Greene Valley Developmental Center, certain employees at each home were authorized to request funds to make purchases for residents and also to arrange field trips. These employees did not always return unspent cash and receipts to the accounting department within five days of taking residents on trips in accordance with the center's policy. Section V, Part C, of the policy states:

> All of the receipts/unused monies along with a copy of the request for funds will be returned to Accounting for verifying within 5 business days of the event.

We reviewed the restricted fund check log for March 2007 and found 51 instances (non-payroll) where the check was outstanding for more than seven days (to allow for weekends), and we reviewed those transactions for compliance with the policy. We determined that two of the transactions were not applicable for our testwork. In 17 of the 49 transactions we tested (35%), residents' monies were outstanding for more than five business days after the day of the event. The days outstanding ranged from 8 to 21 days, and the total amount involved was $886.

When funds of $10.00 or more are given to employees to fulfill requests on behalf of the residents, the employees are required by GVDC's policy to put the money into a safe at the home until it can either be spent or returned to the accounting department. Section V, Part C, of the policy states:

> If for whatever reason the receipts/unused monies totaling $10.00 or more can not be returned to Accounting the same day, the receipts/unused monies are placed in a safe in the home.

In the 51 transactions from March 2007, discussed above, we found 48 transactions in which the amount was $10 or more, and we tested those transactions for compliance with the policy. In 23 of the 48 transactions we tested (48%), the employees did not properly secure the receipts/unused monies in the safes at the homes when more than a day passed before the actual trips were taken with the residents. We also found that some of the homes hadn't started keeping a log to track the money that was put in the safes until late March or in some cases late April 2007. A total of $1,514 of residents' funds was found not to have been secured properly.

Without adequate internal controls over the resident trust accounts, residents' funds could be lost or stolen. When the settlement of funds distributed to employees is delayed, the chances of loss, theft, or inappropriate use increase. The failure to adequately secure funds increases the risk for theft.

Recommendation

The risks identified in this finding should be immediately addressed. The security of residents' funds should become a priority for the Commissioner of the Department of Finance and Administration, the Deputy Commissioner for the Division of Mental Retardation Services, and the Superintendent of Greene Valley Developmental Center. They should determine why the center's employees have been allowed to disregard policies established to safeguard residents' funds. They should assign specific staff the responsibility of ensuring that the established controls are followed. Appropriate disciplinary action should be taken when employees violate control policies.

The Deputy Commissioner should ensure that time limits for funds outstanding are enforced and that all employees follow established procedures for securing receipts/unused monies.

The Deputy Commissioner should ensure that risks such as those noted in this finding are adequately identified and assessed in documented risk assessments at all developmental centers. The Deputy Commissioner should identify specific staff to be responsible for the design and implementation of internal controls to mitigate the risks identified. The Deputy Commissioner should also identify specific staff to be responsible for ongoing monitoring for compliance with all requirements and taking prompt action should exceptions occur.

Management's Comment

Management concurs. GVDC's operating guidelines will be revised to comply with the recommendations of this finding. Additions to the guidelines will include assigning specific responsibility for the monitoring of the safes and safe logs to safeguard the funds that belong to the individuals GVDC serves.

Additional training for the staff of the homes involved in the late return of funds and a change in procedure by one of the homes, which represented 53 percent of late returns, have greatly improved the consistency in having the funds returned on time.

The changes that will be proposed in the GVDC Guidelines will further decrease the incidents of late return of funds. It should be pointed out, however, that the five-day time frame in the GVDC policy was given as guidance to staff with the expectation that, due to unforeseen circumstances such as resident or employee illness, cottage situations/emergencies, lack of transportation or staffing, etc., it could not be met at all times. The seventeen (17) transactions that are exceptions to the five-day guidance noted for resident trips represent only 9.1 percent of the total of 186 similar transactions that were in the restricted fund check log for the month of March. Also, no monies were lost in the noted transactions and, in fact, no resident monies have ever been lost or stolen as a result of either issue mentioned in the audit finding. This would indicate that the internal controls and follow-up actions of the accounting staff have been effective in the prevention of loss.

GVDC did consider the trust funds when completing the 2007 risk assessment for the Center. Specific wording was not added for the trust fund due to the limited amount of time that could be devoted to the process between the training provided for the new documentation method and the date the documentation was due. The Center will add specific wording for the trust fund to the assessment in future years.

PAYMENT CARD USAGE

Our objectives in reviewing controls and procedures over the use of payment cards were to determine whether

- payment card purchases were adequately supported, approved, and reconciled to the monthly bank records;
- cardholder cycle dollar-limit increases were properly justified;
- payment card purchases appeared reasonable and necessary; and
- payment card purchases complied with the Department of General Services' purchasing policies and procedures concerning recurring purchases, purchases from statewide contract, and purchases requiring bids, including purchases that were split to avoid bid requirements.

We reviewed the applicable laws and regulations, interviewed key personnel, and reviewed supporting documentation to gain an understanding of the controls and procedures over payment cards. We tested a sample of payment card transactions for adequate supporting documentation, proper approvals, and reconciliation to the bank records. We reviewed the department's justification for cardholder cycle dollar-limit increases. To determine if purchases appeared reasonable and necessary and to look for possible noncompliance issues, we reviewed payment card transaction listings to look for inappropriate/suspicious vendors, split invoices (multiple purchases from an individual vendor which exceeded $400 over a two-day period for the period ended June 2006 and $2,000 for the period after June 2006), items which exceeded prescribed maximums (transaction limits, daily dollar limits, monthly dollar limits), items purchased on a weekend or holiday, and items which were prohibited by policies and procedures governing payment card purchases. We also tested a sample of purchases for compliance with the Department of General Services' purchasing policies and procedures.

Based on our interviews and our review of supporting documentation, we determined that payment card transactions were adequately supported, approved, and reconciled to the monthly bank records. We determined that the department adequately justified increasing cardholder-cycle dollar limits. We determined that payment card purchases appeared to be reasonable and necessary. We determined that payment card purchases complied with Department of General Services' policies and procedures.

OFFICE OF BUSINESS AND FINANCE

Our objectives in reviewing the controls and procedures of the Office of Business and Finance were to determine whether

- purchases and payments related to employee travel and other reimbursements, supplies, equipment, data and telecommunication services and maintenance, and the Facility Revolving Fund's expenditures were properly approved, adequately supported, accurately computed, and appeared necessary for operations;
- grants to subrecipients were properly monitored; and
- grant payments were properly approved, adequately supported, accurately computed, and allowable.

We reviewed the applicable laws and regulations, interviewed key personnel, and reviewed supporting documentation to gain an understanding of the controls and procedures over purchases and payments for the expenditures mentioned above. We tested nonstatistical samples of purchases and payments for proper approvals, adequate supporting documentation, accuracy, and reasonableness. We determined that these purchases and payments were properly approved, adequately supported, accurately computed, and appeared necessary for operations.

We reviewed the applicable laws and regulations, interviewed key personnel, and reviewed supporting documentation to gain an understanding of the controls and procedures over grant monitoring activities and grant payments. We looked at instances of noncompliance found by the office's internal grant monitoring process during the period July 2005 to January 2007 and reviewed for proper resolutions. We also tested a nonstatistical sample of grant payments for proper approvals, adequate supporting documentation, accuracy, and allowable costs. Based on the procedures performed, we determined that grants to subrecipients were properly monitored, and grant payments were properly approved, adequately supported, accurately computed, and allowable.

MISCELLANEOUS ISSUES

Our objectives were to determine whether

- services for unused telephone lines were terminated in a timely manner;
- wage payments for separated employees were properly discontinued;
- state employees on the state payroll system had valid and active social security numbers;
- interest income for the State Pooled Investment Fund was accurately computed and properly allocated to the participants; and
- the Department of Finance and Administration had assessed the department's risks of errors, fraud, waste, and abuse.

We obtained and tested nonstatistical samples of potentially unused telephone lines belonging to the Department of Finance and Administration and the Division of Mental Retardation Services. We also interviewed responsible employees about the need for continuing the services for these lines. We used a computer-assisted audit technique (CAAT) on the state's payroll and personnel system to identify all wage payments made for the periods after the employees' separation dates, and we selected and reviewed a nonstatistical sample to determine whether the payments were appropriate. We used the results of a CAAT that identified all employees on the state's payroll system who received wages in fiscal year 2006 and whose social security numbers (SSNs) had been identified as belonging to deceased persons by Tennessee Vital Records, a Division of the Department of Health, and we selected and reviewed a nonstatistical sample of these potentially invalid and/or inactive SSNs to determine whether employees' SSNs on the state payroll system were valid and active. We interviewed key personnel and reviewed supporting documentation to gain an understanding of the computation and allocation of interest income from the State Pooled Investment Fund. We also performed a detailed review on a randomly selected calculation and allocation for propriety. We interviewed key personnel and reviewed the department's documentation related to risk assessments.

As a result of our testwork, we determined that the department, including the Division of Mental Retardation Services, did not promptly terminate the services for unused telephone lines as noted in finding 9. Wage payments for separated employees were properly terminated, employees' SSNs were valid and active, and interest income from the State Pooled Investment Fund was accurately computed and properly allocated. We determined that the department, except for the Division of Mental Retardation Services as noted in finding 10, had assessed the department's risks of errors, fraud, waste, and abuse.

9. The Department of Finance and Administration, including the Division of Mental Retardation Services, failed to promptly terminate the service for unused telephone lines, resulting in estimated unnecessary costs to the state of over $3,300 per month

Finding

The Director of the Office of Business and Finance of the Department of Finance and Administration (F&A) and the Information System Manager of the Information Technology section of the Division of Mental Retardation Services (DMRS) were responsible for ensuring that unused telephone lines were disconnected in a timely manner. However, our review showed that the Department of Finance and Administration, including DMRS, incurred estimated unnecessary costs of over $3,300 per month as of May 2007.

We performed a computer-assisted audit technique (CAAT) which identified all telephone lines showing no outgoing long-distance calls during the year ended June 30, 2005. This CAAT identified 293 possibly unused telephone lines belonging to F&A and an additional 100 belonging to DMRS. Our review of 30 of the 293 possibly unused telephone lines from F&A showed that F&A was paying for 14 telephone lines that were not actually in use. The 14 telephone lines included 6 that were no longer being used, one that was no longer in service, and 7 that could not be located by the department. Because of the high error rate in the sample, we asked F&A staff to review all 293 potentially unused telephone lines. The results of their review revealed that 20 of the 293 possibly unused telephone lines had been terminated before our testwork was performed in May 2007, 89 lines had not been terminated as of May 2007 (33%) and were actually unused telephone lines for which the department was currently paying a monthly fee, and 184 lines were currently in use. The payments for the 89 unused telephone lines totaled $2,218 per month.

We also reviewed 10 of the 100 possibly unused telephone lines from DMRS. Our results showed that five of the ten telephone lines were not in use. The five telephone lines included four that were no longer being used and one that could not be located by the division. The payments for the five telephone lines unused by DMRS totaled $159 per month, representing 46% of the $349 total monthly payment of the sample. Given that the monthly payments for the 100 possibly unused telephone lines from DMRS totaled $2,456, the total payment for telephone lines unused by DMRS was estimated to be over $1,100 per month.

Because the department did not have unused telephones disconnected in a timely manner, state funds were wasted.

Recommendation

The Assistant Commissioner of Administration should review all 100 potentially unused telephone lines to determine which ones are inactive, and any inactive lines should be terminated. The Director of F&A's Office of Business and Finance and the Assistant Commissioner of Adminstration should immediately terminate the service for known unused telephone lines and make sure that these terminated telephone lines are no longer included in the monthly billings. The Commissioner should ensure that a control mechanism is put in place to identify telephone lines at F&A, including DMRS, that are no longer needed. These unneeded telephone lines should then be terminated.

Management should ensure that risks such as these noted in this finding are adequately identified and assessed in their documented risk assessment activities. Management should identify specific staff to be responsible for the design and implementation of internal controls to prevent and detect exceptions timely. Management should also identify staff to be responsible for ongoing monitoring for compliance with all requirements and taking prompt action should exceptions occur.

Management's Comment

We concur. The Office of Business and Finance and DMRS Information Technology Section will conduct a thorough review of telephone lines on a regular basis to ensure telephone lines no longer required are promptly disconnected. However, telephone lines for positions expected to the filled in the near future will remain active since the monthly charges incurred will be less than the associated disconnect and reconnect fees.

10. <u>Management of the Division of Mental Retardation Services has not fulfilled its responsibility to formally assess the division's risks of errors, fraud, waste, and abuse</u>

Finding

Management of the Division of Mental Retardation Services has not fulfilled its responsibility to formally assess the division's risks of errors, fraud, waste, and abuse. An ongoing risk assessment process is a basic tenet of internal control.

The 2005 edition of *Governmental Accounting, Auditing, and Financial Reporting* (GAAFR) issued by the Government Finance Officers Association summarizes management's basic responsibilities as follows:

> All managers share certain basic responsibilities, which include: 1) achieving the entity's purpose (effectiveness); 2) making optimal use of scarce resources (efficiency); 3) observing restrictions on the use of resources (compliance); and 4) periodically demonstrating accountability for the stewardship of resources placed in their care (reporting). Internal control

comprises the tools management uses to ensure that it fulfills these important responsibilities.

> A comprehensive framework of internal control must possess five essential elements. It must: 1) provide a favorable *control environment*; 2) provide for the *continuing assessment of risk*; 3) provide for the design, implementation, and maintenance of effective *control-related policies and procedures*; 4) provide for the effective *communication* of information; and 5) provide for the ongoing *monitoring* of the effectiveness of control-related policies and procedures, as well as the resolution of potential problems identified by controls.

The above elements are also mentioned in Statement on Auditing Standards Number 55, as amended, promulgated in April 1988.

The GAAFR explains why this must be a continuous process by stating:

> Changes in a government's circumstances can render once satisfactory control-related policies and procedures inadequate or obsolete. Also, controls have a natural tendency to deteriorate over time unless management properly maintains them. Accordingly, governments must periodically evaluate control-related policies and procedures to determine whether they have been properly designed and implemented and are still adequate and functioning.

Our discussions with management of the Division of Mental Retardation Services disclosed that they have not fulfilled their responsibility to formally assess the division's risks of errors, fraud, waste, and abuse and to document the risk assessment as of the end of our audit, May 31, 2007. This responsibility is of paramount importance, particularly in the complex environment in which the division operates. The Chief Financial Officer provided a "Risk Factor Analysis" worksheet which the division plans to use, but has not yet used in the risk assessment process. The worksheet includes the central office, the three developmental centers, the three regional offices, and the Tennessee Council on Developmental Disabilities. However, we noted that the format of the worksheet needs to be modified because an area could be a high fraud risk and still be considered a low risk overall.

Risks of fraud, waste, and abuse are mitigated by effective internal controls. It is management's responsibility, in addition to performing and documenting a risk assessment, to design, implement, and monitor effective controls in the entity. This too should be an ongoing process.

Recommendation

Management should conduct regular periodic risk assessments. Each assessment should be well documented, complete, and clear. The format of the "Risk Factor Analysis" worksheet should be appropriately modified. The risk assessment process should involve the active participation of staff; however, management is ultimately responsible for the results of the assessment.

The risk assessment should include consideration of the risks of errors, fraud, waste, and abuse related to the Division of Mental Retardation Services. Management should begin with prior audit findings, ensuring that corrective actions recommended by us have been fully implemented. Management should also think about the general types of problems that can occur, such as conflicts of interest in the procurement processes, overbillings, and theft of funds. The relative materiality of the risks should be considered as well. Qualitative as well as quantitative materiality should be considered. The results of the risk assessment should be used by management to design appropriate internal controls to mitigate identified risks. As such, the risks should be prioritized, so that management can focus their initial attention on the greatest risks. Risks and related controls should be clearly linked.

During the next audit, we will review the risk assessment documentation prepared by management. The results of this review will be part of the basis of our conclusions about the control environment of the entity.

Management's Comment

Management does not concur. In June 2007, the division formed its Audit Committee. In August 2007, management conducted a training session for division directors regarding the importance of developing controls and assessing risk in their respective areas. In early fall the Department of Finance and Administration conducted training for all state agencies and supplied the evaluation instruments it wanted agencies to use. Using those instruments, the Division proceeded to conduct its risk assessment and turned in the resulting report to Finance and Administration and the Comptroller's Office ahead of the stated deadline. The division is unaware of any items that did not meet mandated time frames.

It is important to note that even before the current requirements, state agencies were responsible for implementing, monitoring, and updating as needed internal control systems under the requirements of the Financial Integrity Act. Once again, the DMRS turned in all letters and full reviews by the due dates. Many of the controls and assessment of risk done in 2007 as a result of the new requirements had their start in the Financial Integrity Act process. Therefore, management does not agree that it has not fulfilled its responsibilities in this area.

Auditor's Rebuttal

Management stated that it did not concur. Management's stated justification for that position was that the division was in compliance with the Financial Integrity Act. However, the criterion on which we based this finding was not compliance or noncompliance with the Financial Integrity Act. Rather, as stated in the finding, our criteria were the basic tenets of internal control as published by such organizations as the Government Finance Officers Association in *Governmental Accounting, Auditing, and Financial Reporting* and by the

American Institute of Certified Public Accountants in *Statements on Auditing Standards*. Our audit found that the other divisions of the Department of Finance and Administration, including TennCare, had performed acceptable risk assessments during the audit period. In our opinion, the Division of Mental Retardation Services had not.

OBSERVATIONS AND COMMENTS

MANAGEMENT'S RESPONSIBILITY FOR RISK ASSESSMENT

Auditors and management are required to assess the risk of fraud in the operations of the entity. The risk assessment is based on a critical review of operations considering what frauds could be perpetrated in the absence of adequate controls. The auditors' risk assessment is limited to the period during which the audit is conducted and is limited to the transactions that the auditors are able to test during that period. The risk assessment by management is the primary method by which the entity is protected from fraud, waste, and abuse. Since new programs may be established at any time by management or older programs may be discontinued, that assessment is ongoing as part of the daily operations of the entity.

Risks of fraud, waste, and abuse are mitigated by effective internal controls. It is management's responsibility to design, implement, and monitor effective controls in the entity. Although internal and external auditors may include testing of controls as part of their audit procedures, these procedures are not a substitute for the ongoing monitoring required of management. After all, the auditor testing is limited and is usually targeted to test the effectiveness of particular controls. Even if controls appear to be operating effectively during the time of the auditor testing, they may be rendered ineffective the next day by management override or by other circumventions that, if left up to the auditor to detect, will not be noted until the next audit engagement and then only if the auditor tests the same transactions and controls. Furthermore, since staff may be seeking to avoid auditor criticisms, they may comply with the controls during the period that the auditors are on site and revert to ignoring or disregarding the control after the auditors have left the field.

The risk assessments and the actions of management in designing, implementing, and monitoring the controls should be adequately documented to provide an audit trail both for auditors and for management, in the event that there is a change in management or staff, and to maintain a record of areas that are particularly problematic. The assessment and the controls should be reviewed and approved by the head of the entity.

FRAUD CONSIDERATIONS

Statement on Auditing Standards No. 99, *Consideration of Fraud in a Financial Statement Audit,* promulgated by the American Institute of Certified Public Accountants requires auditors to specifically assess the risk of material misstatement of an audited entity's financial statements due to fraud. The standard also restates the obvious premise that management, not the auditors, is primarily responsible for preventing and detecting fraud in its own entity. Management's responsibility is fulfilled in part when it takes appropriate steps to assess the risk of fraud within the entity and to implement adequate internal controls to address the results of those risk assessments.

During our audit, we discussed these responsibilities with management and how management might approach meeting them. We also increased the breadth and depth of our inquiries of management and others in the entity as we deemed appropriate. We obtained formal assurances from top management that management had reviewed the entity's policies and procedures to ensure that they are properly designed to prevent and detect fraud and that management had made changes to the policies and procedures where appropriate. Top management further assured us that all staff had been advised to promptly alert management of all allegations of fraud, suspected fraud, or detected fraud and to be totally candid in all communications with the auditors. All levels of management assured us there were no known instances or allegations of fraud that were not disclosed to us.

TITLE VI OF THE CIVIL RIGHTS ACT OF 1964

Section 4-21-901, *Tennessee Code Annotated*, requires each state governmental entity subject to the requirements of Title VI of the Civil Rights Act of 1964 to submit an annual Title VI compliance report and implementation plan to the Department of Audit by June 30 each year. The Department of Finance and Administration filed its compliance report and implementation plan on June 30, 2006.

Title VI of the Civil Rights Act of 1964 is a federal law. The act requires all state agencies receiving federal money to develop and implement plans to ensure that no person shall, on the grounds of race, color, or origin, be excluded from participation in, be denied the benefits of, or be subjected to discrimination under any program or activity receiving federal funds. The Tennessee Title VI Compliance Commission is responsible for monitoring and enforcement of Title VI. A summary of the dates state agencies filed their annual Title VI compliance reports and implementation plans is presented in the special report *Submission of Title VI Implementation Plans*, issued annually by the Comptroller of the Treasury.

APPENDICES

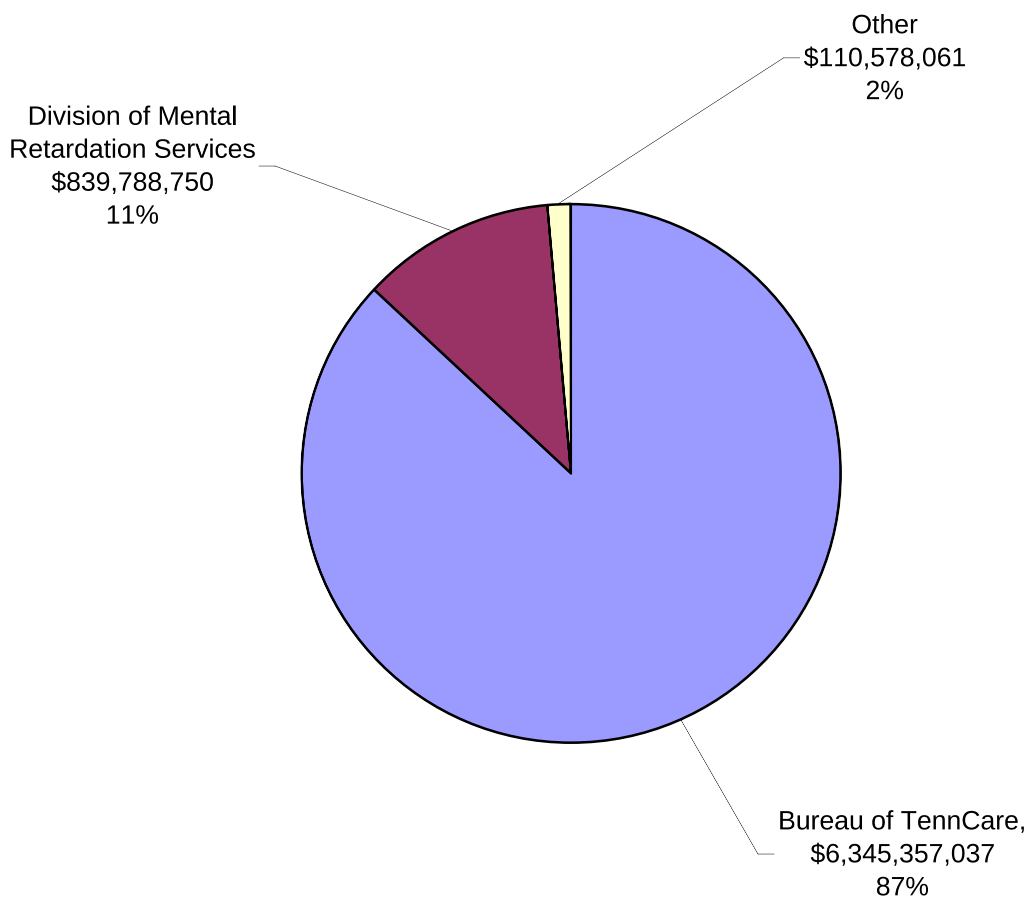
ALLOTMENT CODES

Department of Finance and Administration allotment codes

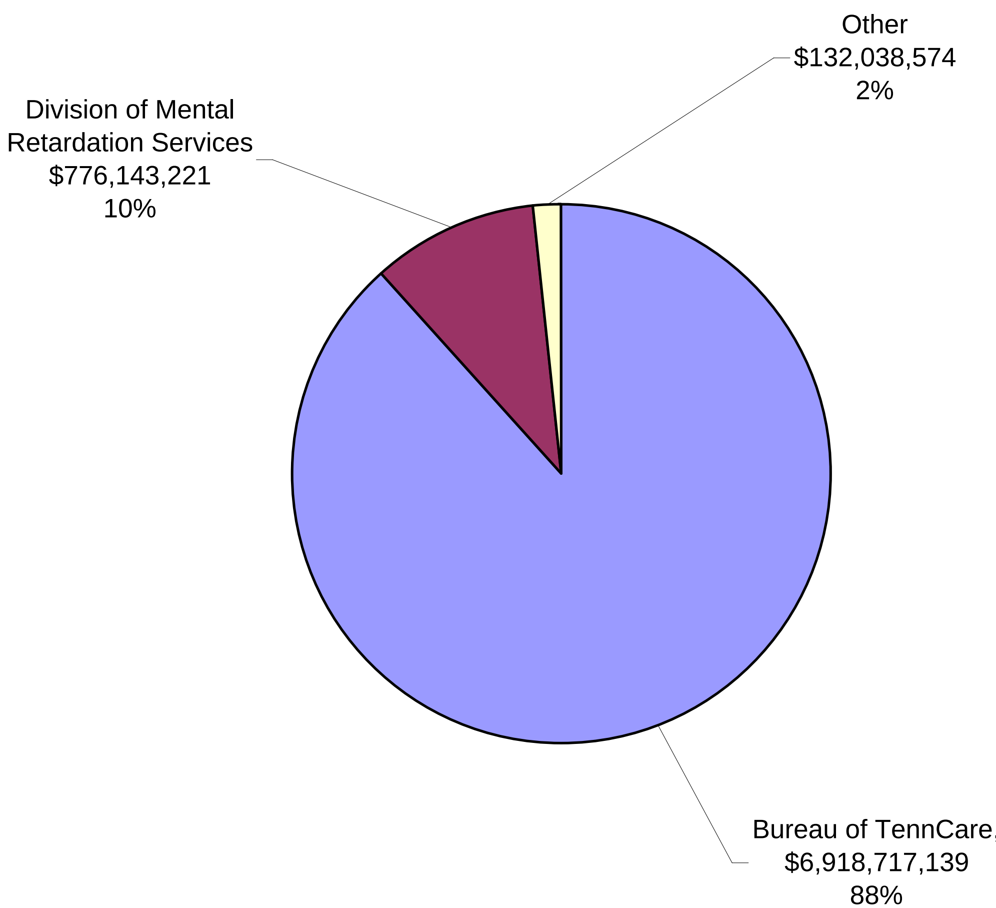
317.01	Division of Administration
317.02	Division of Budget
317.03	Office for Information Resources
317.04	Insurance Administration
317.05	Division of Accounts – Internal Service Fund
317.06	Criminal Justice Programs
317.07	Resource Development and Support
317.10	Real Property Administration
317.11	Commission on National and Community Services
317.12	Office of TennCare Inspector General
317.13	TennCare Advisory Commission
317.15	State Health Planning Division
317.16	Automated Court System Hardware Replacement Loan Fund
317.17	Enterprise Resource Planning
317.18	Division of Shared Services
317.30	Management Information Systems Fund
317.86	Tennessee Insurance System
317.90	Private Purpose Trust Funds
317.97	Telephone Billing
317.99	Division of Accounts – Other
318.01	Office of Health Services
318.65	TennCare Administration
318.66	TennCare Services
318.67	Waivers and Crossover Services
318.68	Long-Term Care Services
318.80	TennCare-Governor’s Office of Children’s Care Coordination
344.01	Mental Retardation Administration
344.02	Community Services
344.10	Arlington Developmental Center
344.11	Clover Bottom Developmental Center
344.12	Greene Valley Developmental Center
344.20	West Tennessee Regional Office
344.21	Middle Tennessee Regional Office
344.22	East Tennessee Regional Office
344.50	Major Maintenance
344.81	Developmental Disabilities Council
350.30	Cover Tennessee Health Care – CoverTN

350.40 Cover Tennessee Health Care – AccessTN
350.50 Cover Tennessee Health Care – CoverKids
350.60 Cover Tennessee Health Care – CoverRX
350.70 Cover Tennessee Health Care – Diabetes Prevention and Health Improvement
350.80 Cover Tennessee Health Care – Health Care Safety Net

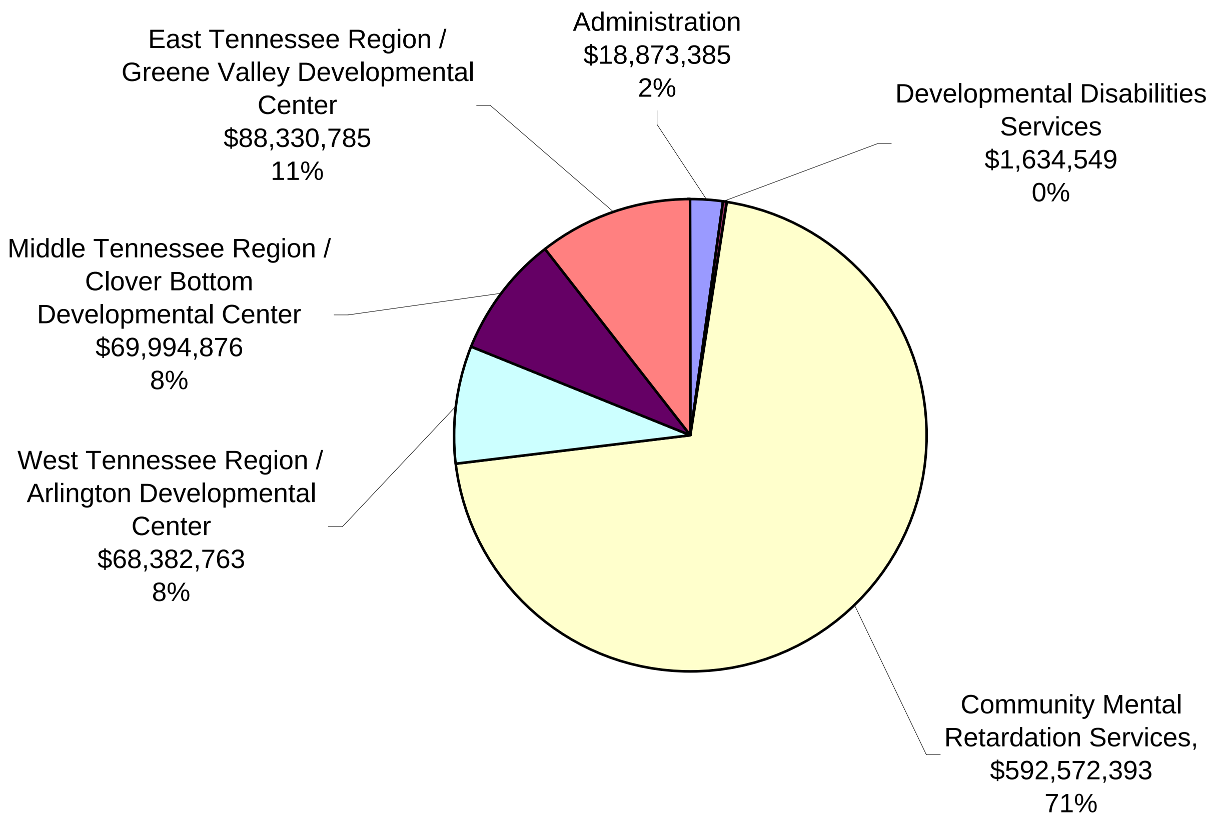
Department of Finance and Administration
General Fund Expenditures
Fiscal Year Ended June 30, 2007 (Unaudited)



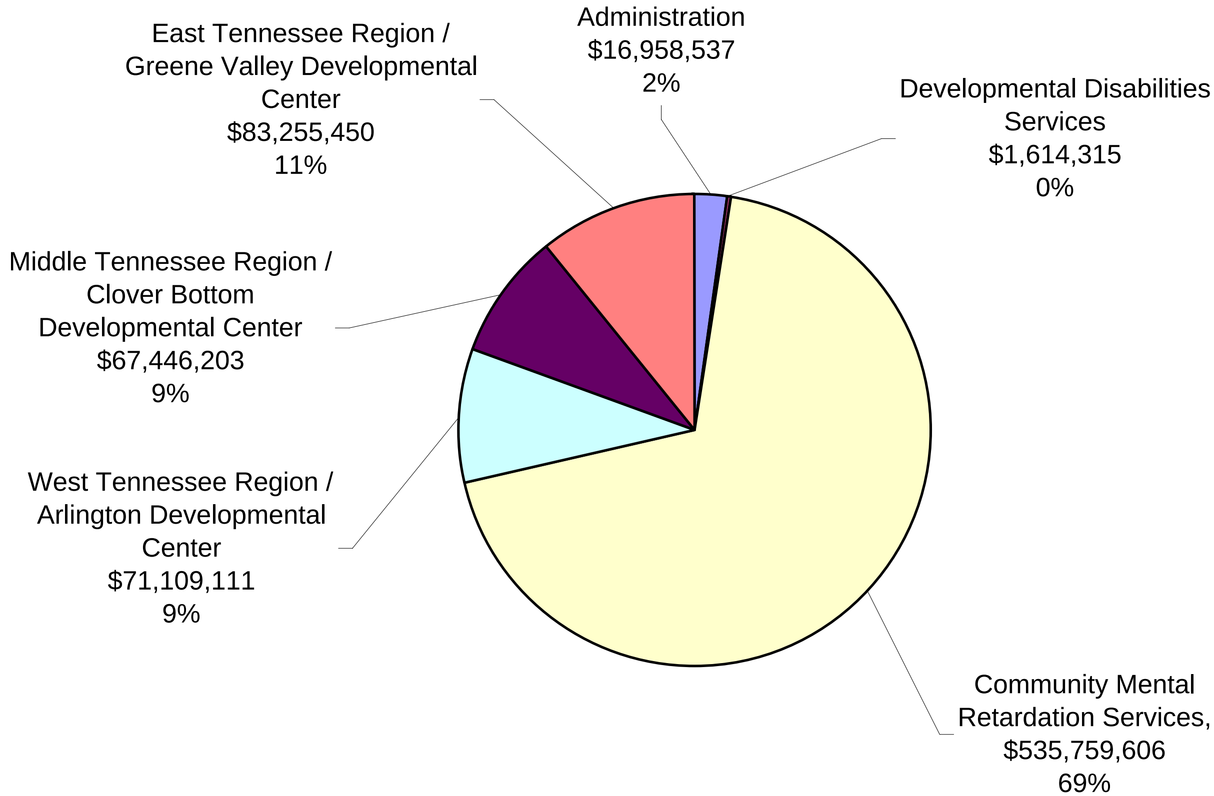
Department of Finance and Administration
General Fund Expenditures
Fiscal Year Ended June 30, 2006 (Unaudited)



Division of Mental Retardation Services
Expenditures
Fiscal Year Ended June 30, 2007 (Unaudited)



Division of Mental Retardation Services
Expenditures
Fiscal Year Ended June 30, 2006 (Unaudited)



MANAGEMENT'S COMMENTS FROM PRIOR AUDITS

Current Finding

<u>The Division of Mental Retardation Services still had inadequate controls over the contract with the Community Services Network of West Tennessee, hampering the division's ability to properly administer the contract</u>

Management's Comment

For the Year Ended June 30, 2003

We concur that the contract arrangement with Community Services Network is problematic. We are currently in negotiations with the agency to re-evaluate the form and substance of the contract and to redesign the payment methodology. The Division is eager to rectify any questionable practices and will investigate and address any such issues in regard to the CSN contract or any other agreement.

Current Finding

<u>The Division of Mental Retardation Services has still failed to collect available federal reimbursement for waiver services, costing state taxpayers millions of dollars</u>

Management's Comment

For the Year Ended June 30, 2003

We concur. We are restructuring the Office of Administrative Services to allow an intensive reconciliation process to be performed and all denied claims resubmitted for reimbursement.

Current Finding

<u>The Division of Mental Retardation Services still had improper employer-employee relationships, raising serious policy and legal issues</u>

Management's Comments

For the Year Ended June 30, 2003

We concur. Contract policies have been changed to require re-evaluation of each contract and an effort made to convert any possible contractor positions to state employees. This has resulted in a conversion in the current fiscal year of approximately 25 positions. The Division has been instructed to closely review each contract for possible conversion or reduction.

For the Year Ended June 30, 2002

We concur in part: We recognize that the situation of contracting for staff and having contract staff as supervisors is not optimal. However, with the requirements placed upon this region by the Federal Courts we have not been able to create and fill the number and types of positions required for compliance. Fines for non-compliance have been levied on the State in the past at $1,000.00 per day.

The specialty staff requirement in the remedial court order deals with not only numbers of staff, but qualifications. For example, we must have Speech Pathologists that have specialty training in swallowing and serve as swallowing therapists; Physicians, Nurses, Behavioral Analysts and Therapists such as PT and OT, with specific training and experience working with the MR or DD population, etc. DOP qualification requirements do not address these additional qualifications for this specialty population. There is not an established position series for Behavioral Analysts.

A few years ago a proposal was made to create the numbers and types of positions required and that proposal was rejected by F & A because it was too costly and would have to be done statewide, not just for this region.

Requests for Proposals (RFP) for each of these contracted services are in Nashville awaiting approval.