
Follow-Up Report on a Financial Audit of the Department of Human Services

A Report to the
Governor
and the
Legislature of
the State of
Hawaii



THE AUDITOR
STATE OF HAWAII

The Office of the Auditor

The missions of the Office of the Auditor are assigned by the Hawaii State Constitution (Article VII, Section 10). The primary mission is to conduct post audits of the transactions, accounts, programs, and performance of public agencies. A supplemental mission is to conduct such other investigations and prepare such additional reports as may be directed by the Legislature.

Under its assigned missions, the office conducts the following types of examinations:

1. *Financial audits* attest to the fairness of the financial statements of agencies. They examine the adequacy of the financial records and accounting and internal controls, and they determine the legality and propriety of expenditures.
2. *Management audits*, which are also referred to as *performance audits*, examine the effectiveness of programs or the efficiency of agencies or both. These audits are also called *program audits*, when they focus on whether programs are attaining the objectives and results expected of them, and *operations audits*, when they examine how well agencies are organized and managed and how efficiently they acquire and utilize resources.
3. *Sunset evaluations* evaluate new professional and occupational licensing programs to determine whether the programs should be terminated, continued, or modified. These evaluations are conducted in accordance with criteria established by statute.
4. *Sunrise analyses* are similar to sunset evaluations, but they apply to proposed rather than existing regulatory programs. Before a new professional and occupational licensing program can be enacted, the statutes require that the measure be analyzed by the Office of the Auditor as to its probable effects.
5. *Health insurance analyses* examine bills that propose to mandate certain health insurance benefits. Such bills cannot be enacted unless they are referred to the Office of the Auditor for an assessment of the social and financial impact of the proposed measure.
6. *Analyses of proposed special funds* and existing *trust and revolving funds* determine if proposals to establish these funds and existing funds meet legislative criteria.
7. *Procurement compliance audits* and other *procurement-related monitoring* assist the Legislature in overseeing government procurement practices.
8. *Fiscal accountability reports* analyze expenditures by the state Department of Education in various areas.
9. *Special studies* respond to requests from both houses of the Legislature. The studies usually address specific problems for which the Legislature is seeking solutions.

Hawaii's laws provide the Auditor with broad powers to examine all books, records, files, papers, and documents and all financial affairs of every agency. The Auditor also has the authority to summon persons to produce records and to question persons under oath. However, the Office of the Auditor exercises no control function, and its authority is limited to reviewing, evaluating, and reporting on its findings and recommendations to the Legislature and the Governor.



THE AUDITOR STATE OF HAWAII

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Submitted by

THE AUDITOR
STATE OF HAWAII

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State Auditor

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Introduction

The Office of the Auditor issues a wide variety of reports and studies recommending improvements in government operations. In response to growing interest in the impact of our audits, we have expanded our follow-up program to include a systematic review of selected findings and recommendations of previous audit reports. We revisit the subject agencies to verify and assess any progress made in addressing prior audit findings and recommendations. Government auditing standards require an audit follow-up process to determine whether an auditee has taken timely and appropriate corrective actions on findings and recommendations from previous reports.

The purpose of this report is to describe actions taken by the governor and the Department of Human Services (DHS) with respect to certain recommendations in our January 1994 report, *Financial Audit of the Department of Human Services*, Report No. 94-5. We hope that the information provided in this report will assist policy makers in ensuring effective, efficient, and accountable programs.

Background

DHS administers programs designed to improve people's social well-being and productivity. These programs include family, child, and adult welfare, economic assistance, health care assistance, rehabilitation toward self care, public housing, and others. Our 1994 audit report covered the fiscal year July 1, 1992 to June 30, 1993. We conducted the audit together with the certified public accounting firm of KPMG Peat Marwick LLP.

The magnitude of the deficiencies we found in our 1994 report reflected an overall failure of stewardship by DHS management. The financial operations of the department were not being implemented in a responsible manner. We found significant deficiencies in DHS's financial accounting and internal control practices and procedures that resulted in seven "reportable conditions." We found that DHS was:

- repeatedly and deliberately circumventing state laws and fiscal controls by improperly charging expenditures of certain programs to appropriations meant for other programs in order to cover cash shortages;
- failing to lapse federal reimbursements into the State's general fund as required by law and instead using a portion of these funds to finance program expenditures not authorized by the Legislature;

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- not systematically tracking and recovering welfare overpayments;
 - not maximizing federal funding available for child care programs due to errors and delays;
 - not reconciling or replenishing welfare imprest bank accounts as needed;
 - using questionable encumbrances to avoid lapsing; and
 - not completing reviews of subrecipients.

We noted several other weaknesses involving DHS's internal controls and operations. Weaknesses included:

- medicaid budget requests which did not reflect all projected program costs;
- controls over income maintenance programs could improve;
- computer controls relating to security and program changes to data files were not implemented and certain computer equipment was significantly underutilized;
- the cost allocation process was inefficient and susceptible to error;
- payments for real property leases may have been improper;
- problems relating to vacant positions were not identified and corrected; and
- DHS's Evaluation Office could be better used to improve program operations, financial management, and internal controls.

Our 1994 report concluded that these problems could not be fixed overnight. Correcting the deficiencies would demand a concerted effort at the very top levels of DHS and state government. We called for the governor's direct involvement, made a number of specific recommendations for improvement, and suggested that the director of human services appoint a task force to plan for addressing the deficiencies.

Approach to Follow-Up

As a follow-up of our 1994 report, we reviewed the governor's letter to the Auditor of November 18, 1994, which provided information concerning actions taken on our recommendations. The letter included reports from both DHS and a task force appointed by the governor to address the issues we raised. (We will refer to the letter and the reports collectively as "the governor's letter.")

Together with KPMG Peat Marwick LLP, we conducted fieldwork at the department to gather additional information necessary for this report. Our work was performed from January 1995 through April 1995.

The following is our overall assessment of progress made, followed by a description of each of our previous recommendations, actions reported in the governor's 1994 letter to us, and the results of our recent fieldwork.

Summary of Follow-Up

Our overall assessment is that the Department of Human Services has made progress in implementing our recommendations to properly charge appropriations, lapse federal reimbursements, maximize federal reimbursements, reconcile bank accounts as needed, avoid questionable encumbrances, submit realistic budgets, develop better controls for data processing, maintain a schedule of real property leases, reduce employee vacancies, and better use its Evaluation Office.

However, DHS has not made significant progress on our recommendations to properly manage welfare overpayments, replenish its imprest accounts, review subrecipients on time, better control its income maintenance program, and improve its cost allocation process. The department has not formalized a plan for correcting the deficiencies we found.

Recommendation from 1994 Report

In our 1994 report we recommended that the governor charge the director of human services, the comptroller, and the director of finance with the responsibility for ensuring that DHS adheres to state budgeting and accounting requirements on allotments, charging of appropriations, lapsing, and encumbrances.

Implementation as reported in the governor's letter

In his November 1994 letter to the Auditor, the former governor stated that he appointed a task force comprised of the directors of DHS, the Department of Accounting and General Services (DAGS), and the Department of Budget and Finance (B&F) to address the pertinent issues in our report.

Results of our fieldwork

In our follow-up fieldwork, we found that the governor did appoint a task force and charged the director of human services, the comptroller, and the director of finance with the responsibility of addressing the recommendations in our report.

**Recommendation
from 1994 Report**

We recommended in 1994 that DHS cease immediately the mischarging of appropriations.

***Implementation as
reported in the
governor's letter***

The governor's letter indicated that DHS has implemented procedures to ensure compliance with proper accounting and fiscal procedures for charging program expenditures to appropriate accounts.

Results of our fieldwork

In our follow-up, we found that the practice of mischarging appropriations continued into FY1993-94 and that no records were maintained to monitor these mischarges. However, the extent and amount of mischarges significantly decreased from an estimated \$23.3 million in FY 1992-93 to \$1.2 million in FY1993-94. We found no evidence of mischarges after November 1993.

**Recommendation
from 1994 Report**

In 1994 we recommended that the department lapse federal reimbursements to the State's general fund. (Lapsing of federal reimbursements means returning to the general fund the federal government's share of social services and welfare payments made by the State.)

***Implementation as
reported in the
governor's letter***

According to the governor's letter, the department had lapsed \$36.9 million in federal reimbursements to the general fund as of November 17, 1994. In July 1994, DHS implemented uniform lapsing procedures including a quarterly schedule with activity completion dates.

Results of our fieldwork

We found that as of December 1994, all federal reimbursements pertaining to FY1992-93 or earlier were accounted for and lapsed to the general fund. In March 1995, the balance of federal reimbursements relating to FY1993-94 was lapsed to the general fund.

**Recommendation
from 1994 Report**

We recommended in 1994 that the department identify information it needs to develop and implement a system to properly record and process welfare overpayments.

***Implementation as
reported in the
governor's letter***

The governor's letter reported that DHS formed a Management Recovery Team to present recommendations to the DHS director regarding the overpayment recovery system. Consequently, a plan for the redesign of the department's Automated Recovery System (ARS) was developed. The plan will not be implemented until June 30, 1995.

The governor's letter also reported that the department does not currently have the resources to develop a new interface between the ARS and the Hawaii Automated Welfare Information system (HAWI) as recommended by the Management Recovery Team. However, the department's Information Services Office (ISO) has committed to remedy the interface problems by June 30, 1996.

Results of our fieldwork

Our follow-up found continued problems in the monitoring and collection of welfare overpayments. Although DHS has formulated a corrective action plan, the plan has not been implemented and DHS's records continue to be inadequate, thus preventing management from monitoring, evaluating, and collecting all outstanding welfare overpayments.

DHS has initiated steps to identify and fix the computer systems' interface problems. However, we found that discrepancies between information contained in the ARS and HAWI systems still have not been reconciled due to staffing constraints.

**Recommendation
from 1994 Report**

We recommended in 1994 that the department make timely and accurate claims for federal reimbursements.

***Implementation as
reported in the
governor's letter***

The governor's letter indicated that DHS has developed formal and uniform accounting procedures for federal fund monitoring, drawdowns, and reclassifications. The department is pursuing efforts to specifically identify federal funds on a grant by grant basis. Training on federal funds was provided to program, branch, and fiscal staffs.

Results of our fieldwork

We found that DHS has improved its procedures for monitoring federal grants and processing accurate reimbursement requests. It is now correctly coding expenditures for child care costs so that federal reimbursements can be obtained. In addition, the department is doing a better job of identifying programs that qualify for federal reimbursement.

**Recommendation
from 1994 Report**

We recommended in 1994 that the department reconcile and replenish its bank accounts as required.

***Implementation as
reported in the
governor's letter***

According to the governor's letter, the department is maintaining the reconciliation of all the imprest bank accounts on a current basis.

Results of our fieldwork

We found that imprest bank account balances are now being reconciled to the check register balances. However, imprest accounts are not being replenished as required by law.

**Recommendation
from 1994 Report**

We recommended in 1994 that the department cease making questionable encumbrances. (These encumbrances included using purchase orders to encumber funds when there were no firm commitments to purchase goods or services.)

***Implementation as
reported in the
governor's letter***

The governor's letter reported that DHS issued budget execution policies on the proper review and authorization of encumbrances. Staff were also reminded of the procedural requirements regarding the appropriate supporting documentation and approvals for purchase order encumbrances.

Results of our fieldwork

We found that questionable encumbrances are no longer being made.

**Recommendation
from 1994 Report**

In 1994 we recommended that the department perform timely reviews of subrecipients. (Subrecipients are agencies that DHS contracts with to provide certain services with federal funds.)

***Implementation as
reported in the
governor's letter***

The governor's letter said that DHS has completed more than 19 subrecipient reviews. The department has also developed an interim action policy for subrecipient audit review. Monitoring procedures for

purchase of service contracts have been drafted and implementation is expected by July 1995.

Results of our fieldwork

We found that DHS is trying to perform timely reviews of subrecipients. However, DHS still does not have a comprehensive list of subrecipients. Without this list, the department cannot determine how many subrecipients are delinquent in submitting their required audit reports for the department's review.

**Recommendation
from 1994 Report**

We recommended that the department present realistic budgets to the Legislature based on expected costs.

***Implementation as
reported in the
governor's letter***

The governor's letter indicated that for the fiscal biennium 1995-97, the base budget and additional requests for the Medicaid and QUEST programs have been submitted to the Department of Budget and Finance for review. The submitted budget reflects total anticipated program costs.

Results of our fieldwork

We found that DHS had to submit emergency budget requests for both FY1993-94 and FY1994-95. However, our review of budget documents suggests that DHS submitted to the 1995 Legislature what it believes to be a realistic budget, based on expected costs.

**Recommendation
from 1994 Report**

We recommended that the department develop better controls for its income maintenance programs and data processing. (Better controls meant checking data entry for accuracy, standardizing documentation in case files, and verifying residency of welfare recipients. Also, improvements were needed in the income verifying and reporting process in conformity with federal regulations. Improved controls required for data processing included utilizing existing system security procedures and better utilizing the new computer.)

***Implementation as
reported in the
governor's letter***

The governor's letter indicated that the department does not concur with all of our 1994 findings and recommendations concerning controls for income maintenance programs. While DHS is planning administrative initiatives to enhance program management, it has taken no actions in response to most of the deficiencies cited in our 1994 audit. DHS is monitoring its Program Development-Income Maintenance Section and sending reminders to units that are not timely in submitting income verification reports.

The governor's letter also reported that DHS is currently utilizing three of the four security products in the HAWI system. The fourth product, which protects against program access to the files, is not needed in HAWI's dedicated mainframe environment. The letter responded that to review the large volume of information available on the Program Log Extract Utility (PLEU) log is impractical. Staff of the Information Systems Office (ISO) and the Information and Communication Services Division (ICSD) will continue to define and refine criteria applicable to extracting PLEU records for daily reporting and review. DHS plans to complete the migration of the Accounts Recovery System (ARS) from the S/36 to the AS/400 computer by June 30, 1995, making better use of the AS/400's capabilities.

Results of our fieldwork

For the income maintenance program, we found DHS has not taken corrective actions concerning the completeness and accuracy of data entry, the documentation within case files, and residency verification of welfare recipients and their dependents. Welfare units are still not properly preparing and submitting report forms for the Income Eligibility Verification System (IEVS) in conformity with federal regulations.

Concerning better controls for its data processing, DHS continues to underutilize its AS/400 minicomputer. However, the department is currently using the applicable internal security products on its HAWI system. Also, DHS is currently developing criteria to be used in extracting a more meaningful and manageable set of data. This data will be used in producing exception reports which can then be used in monitoring the system's most sensitive data.

**Recommendation
from 1994 Report**

We recommended in 1994 that the department improve its cost allocation process. (Cost allocation means allocation of overhead and other costs to federally funded programs.)

***Implementation as
reported in the
governor's letter***

The governor's letter indicated that finding a software package to allocate costs as we recommended may not be feasible because DHS allocates cost differently from other government and private accounting methods. However, as an interim measure, DHS plans to upgrade additional personal computers and redistribute the accounting workload to increase clerical support to the accountants during the cost allocation periods. This will reduce preparation time and allow a greater opportunity for supervisory review before the federal report deadline.

Results of our fieldwork

We found that DHS has attempted to improve the cost allocation process through reassignment of staff. However, the cost allocation process remains relatively unchanged from our prior report.

**Recommendation
from 1994 Report**

We recommended that the department maintain a schedule of its real property leases.

***Implementation as
reported in the
governor's letter***

The governor's letter reported that DHS will continue to maintain an updated list of office space leases. In addition, DHS and DAGS have reached a final determination on the lease rent amounts budgeted and paid by DAGS.

Results of our fieldwork

We found that DHS is now maintaining a schedule of the department's real property leases and is paying those rents for which it is responsible.

**Recommendation
from 1994 Report**

We recommended that DHS work with other agencies to reduce vacancies in the department.

***Implementation as
reported in the
governor's letter***

The governor's letter indicated that DHS continues to work with the Department of Human Resources Development (DHRD) in facilitating the filling of vacancies, especially for critical positions such as social service assistants. A review of the current vacancy level must take into consideration the position restriction for DHS in FY1994-95.

Results of our fieldwork

We found that DHS has been working with other agencies to reduce vacancies in the department. This includes working with the Department of Human Resources Development and the Department of Budget and Finance.

**Recommendation
from 1994 Report**

We recommended that DHS make better use of staff in its Evaluation Office.

***Implementation as
reported in the
governor's letter***

The governor's letter indicated that DHS does not agree with the finding that the Evaluation Office (EVO) is not fully utilized. Program and management evaluation staff continue to perform program and management studies for DHS divisions and attached agencies upon request. Financial evaluation staff will pursue the subrecipient audit reviews as necessary.

Results of our fieldwork

We found that DHS has made some progress in making better use of staff in its Evaluation Office, including conducting reviews of selected programs and operations in the department.

**Recommendation
from 1994 Report**

We recommended that the director of human services appoint a task force to develop a plan to address deficiencies uncovered in our audit. The plan should set priorities for implementation of corrective measures and timetables for implementation.

***Implementation as
reported in the
governor's letter***

The governor's letter did not respond to this recommendation.

Results of our fieldwork

We found that the governor appointed a task force to address deficiencies uncovered in the audit report. While the department is addressing most of our recommendations, no plan has been formalized for the implementation of corrective measures and timetables.

Conclusions

The governor and the Department of Human Services have taken steps to correct many of the more significant deficiencies noted in our previous financial audit. For example, the improper charging of expenditures of certain programs to appropriations of other programs appears to have ended.

The department lapsed federal reimbursements relating to FY1992-93 and FY1993-94 to the general fund.

Much remains to be done, particularly in establishing procedures to ensure the completeness and accuracy of data entry, documentation in case files, and verifying the residency of recipients of assistance. We urge the department to reconsider its resistance to establishing controls over the processes of data collection, verification, and entry. We believe these controls are essential to provide assurance that welfare payments are made in the proper amounts to those who can clearly demonstrate need.

Since expenditures for social services programs consume almost 20 percent of the State's operating budget—more than \$800 million annually—the Department of Human Services is responsible for instituting proper accounting controls and adequate monitoring procedures to help ensure that these public moneys are spent as intended.

