



State Auditor's Annual Report



Report on Internal Control
Over Financial Reporting
And Compliance And Other Matters
State of Vermont Management Letter
Fiscal Year June 30, 2004

Randolph D. Brock
Vermont State Auditor
March 31, 2005

Mission Statement

The mission of the Auditor's Office is to be a catalyst for good government by promoting reliable and accurate financial reporting as well as promoting economy, efficiency and effectiveness in State government.

COVER:

“Wenlock, Vermont, 1943”

by Benjamin Gates
Auditor of Accounts, State of Vermont
1917 – 1941

Donated to the State by Jan R. Westervelt of Cabot, Vermont

State Auditor's Annual Report

Report on Internal Control
Over Financial Reporting And Compliance
And Other Matters
State of Vermont Management Letter

Table of Contents

State Auditor's Annual Report	1
Report On Internal Control Over Financial Reporting And Compliance And Other Matters	4
Administration's Response To Auditor's Report On Internal Control Over Financial Reporting And Compliance And Other Matters	10
Administration's Response To 2004 Single Audit Report Findings	19

This page intentionally left blank.



**STATE OF VERMONT
OFFICE OF THE STATE AUDITOR**

State Auditor's Annual Report

Speaker of the House of Representatives Gaye Symington
President Pro-Tempore of the Senate Peter F. Welch
Governor James H. Douglas

Dear Colleagues,

I am pleased to report to you that Vermont continues to make progress in improving the timeliness and accuracy of its financial reporting. Today, for the first time in three years, the State of Vermont has completed the audit of its financial statements by the statutory deadline. Our opinion on those statements is an unqualified one. However, despite this positive achievement, there remains work to be done to improve the quality of the State's internal controls, financial reporting, and compliance with federal requirements.

Report on Internal Control and Compliance Overview

Our Report on Internal Control Over Financial Reporting and Compliance and Other Matters is related to our audit of the State's basic financial statements for the fiscal year ending June 30, 2004. This report found five reportable conditions, four of which were deemed to be material weaknesses because of their seriousness.

Agency of Transportation Capitalization Issues: During the preparation of the 2004 financial statements, management at the Agency of Transportation determined that its capitalization policy for infrastructure assets such as roads and bridges was not consistently applied. As a result, the 2004 financial statements were restated to remove approximately \$92 million of projects owned by local municipalities and improperly recorded as State assets, and to capitalize approximately \$94 million of prior year infrastructure expenditures which had been expensed in error. Although the net effect of these items was not material, the size and nature of the individual errors are troubling.

Subrecipient Monitoring: Prior annual audit reports have raised concerns about weaknesses in the State's compliance with federal regulations requiring it to monitor federal funds which are passed on by State agencies to local governments, non-profit organizations and similar subrecipients. This year there has been significant

improvement in subrecipient monitoring, but much work in the area remains to be done. While these same requirements are not mandatory for the proper control over State-funded grants, sound fiscal management would indicate that policies, procedures, and controls should be in place to ensure that the expenditure of State funds are in accordance with State laws and regulations.

Absence of Linkage Between Authorization and Expenditure: There continues to be little accountability to match services provided to the proper fiscal year. Thus, expenditures are not necessarily aligned properly by period with their respective authorizations. This can result in budgetary manipulation that will not be detected by State employees.

Manual and Complex Reconciliation Process: The State's accounting process is very decentralized and a substantial portion of this process is still compiled manually. While the Department of Finance and Management has made significant improvements in the underlying processes, more is needed. Since the State has not mandated use of VISION, the State's centralized accounting system, across government, the reliance upon manual reconciliation to VISION continues to delay the production of timely financial statements and to pose risk of error. In addition, the reliance by the department on one individual for much of this work creates a potential single point of failure.

A material weakness occurs where there is risk that material misstatements caused by error or fraud may occur and not be detected timely by employees within the normal course of business.

Federal Single Audit Overview

Our compliance audit of the State's major federal programs disclosed 12 material weaknesses, down substantially from the 27 material weaknesses in 2003. This decline in part results from improvements by the Administration in federal subrecipient monitoring, although six (versus 13 last year) of 2004's weaknesses relate to this issue. Three other material weaknesses relate directly to systemic issues of reconciliation between VISION and other legacy systems still in use, mirroring the findings described above.

A material weakness in this type of compliance audit is a condition evidencing material risk of noncompliance with the applicable requirements of laws, regulations, contracts, and grants that may not be detected timely by responsible employees.

Improvements Made, Improvements Needed

Although this year the State was able, just barely, to produce timely financial statements, the process of doing so was not without difficulty. Continued improvement in automation, building more capacity and depth into the Department of Finance and Management and demanding improved accuracy in reconciliations from departments and agencies, especially the Agency of Transportation, are all required. Subrecipient monitoring, though improved, continues to

represent a substantial risk, as more and more money, both federal and State, is passed on to others to manage on behalf of government. What is encouraging is the evident commitment by financial managers throughout State Government. The results this year demonstrate substantial improvement from prior years, and offer a promise of continued improvement in the year ahead.

The success in completing the Comprehensive Annual Financial Report on time rests with Jim Reardon and Rob Hofmann, the present and former Commissioners of Finance and Management, respectively, and their staff; the State Treasurer, Jeb Spaulding, and his staff; the partners and staff of KPMG LLP and the staff here at the State Auditor's Office. Their dedication, focus and extra effort are to be commended.

Sincerely,

A handwritten signature in black ink, appearing to read "R. Brock", is positioned to the left of a vertical red line.

Randolph D. Brock
State Auditor

March 31, 2005



RANDOLPH D. BROCK
STATE AUDITOR
STATE OF VERMONT
OFFICE OF THE STATE AUDITOR



PO BOX 564
BURLINGTON, VT 05402

**Report on Internal Control Over Financial Reporting and On Compliance and
Other Matters Based on An Audit of Financial Statements Performed
in Accordance With *Government Auditing Standards***

Speaker of the House of Representatives Gaye Symington
President Pro-Tempore of the Senate Peter F. Welch
Governor James H. Douglas
State House
Montpelier, Vermont

The State Auditor has audited the financial statements of the governmental activities, the business-type activities, the aggregate discretely presented component units, each major fund, and the aggregate remaining fund information of the State of Vermont, as of and for the year ended June 30, 2004, and has issued a report thereon dated March 31, 2005. The State Auditor conducted the audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

The State Auditor did not audit the financial statements of certain entities included in the reporting entity of the State of Vermont. Those financial statements were audited by other auditors who issued separate reports on internal control over financial reporting and compliance and other matters in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*. The financial statements of the State Environmental Revolving Fund (consolidated with the Federal Revenue Fund) and the Vermont Sustainable Jobs Fund (a discretely presented component unit), were not audited in accordance with *Government Auditing Standards* and, accordingly, this report does not extend to those funds.

Internal Control Over Financial Reporting

In planning and performing the audit, the State Auditor and KPMG LLP jointly considered the State of Vermont's internal control over financial reporting in order for the State Auditor to determine auditing procedures for the purpose of expressing the opinion on the basic financial statements referred to above and not to provide assurance

132 State Street • Montpelier, Vermont 05633-5101
Auditor: (802) 828-2281 • Toll-Free (in VT only): 1-877-290-1400 • Fax: (802) 828-2198
email: auditor@sao.state.vt.us • website: www.state.vt.us/sao

on internal control over financial reporting. However, certain matters involving internal control over financial reporting and its operation were noted that were considered to be reportable conditions. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of internal control over financial reporting that, in our judgment, could adversely affect the State of Vermont's ability to record, process, summarize and report financial data consistent with the assertions of management in the basic financial statements. The reportable conditions noted are described below:

Agency of Transportation Capitalization Issues

The preparation of financial statements in accordance with accounting principles generally accepted in the United States of America requires governmental entities to record and report capital assets. Capital assets include infrastructure assets such as roads and bridges. The assumptions underlying the capitalization of capital assets require that management establish policies, procedures and controls to record projects meeting its capitalization policy.

During 2003, management at the Agency of Transportation (AOT) reported its investment in infrastructure. During the preparation of the 2004 financial statements, management at AOT determined that its capitalization policy was not consistently applied. Specifically, management at AOT determined the following:

- A number of infrastructure projects were recorded as either capital assets or work in process at June 30, 2003. Additional costs were added to the projects during fiscal 2004. Management subsequently determined that ownership of these projects did not vest with the State of Vermont. Rather, these projects are owned by local municipalities throughout the State. As a result of this error, the 2004 financial statements were restated to remove approximately \$92 million of projects owned by the local municipalities.

- Concurrent with AOT's more thorough review of open construction projects, management determined that certain prior year infrastructure expenditures were not capitalized in accordance with the State's accounting policy. This required a restatement of the 2004 financial statements to capitalize approximately \$94 million of such expenditures.

The failure to consistently apply its capitalization policy and to ensure the accuracy of the information required to prepare complete and accurate financial statements constitutes a material weakness. Management should ensure its capitalization policy is consistently applied. This may require an evaluation of the front-end processes and controls in place to establish projects in the accounting system. Appropriate consideration should be given to ensure that personnel with the requisite skills and knowledge of both project management and accounting are involved.

Subrecipient Monitoring

In accordance with OMB Circular A-133, the State is required to adhere to laws and regulations pertaining to federal financial assistance programs administered by the State. While these same requirements are not mandatory for the proper control over State-funded grants, sound fiscal management would indicate that policies, procedures, and controls should be in place to ensure the expenditure of State funds are in accordance with State laws and regulations. Once a subrecipient relationship is created, the State has a responsibility to ensure that the subrecipient is made aware that it has been awarded State funds through a grant agreement and to determine whether or not the subrecipient has spent the awarded funds in accordance with State regulations by implementing and performing procedures to monitor the grant activities of the subrecipient. Through the results of procedures performed during the audit of the financial statements, we have determined that adequate procedures to ensure that the appropriate use of State pass-through funds is monitored do not exist. These requirements are similar to the requirements imposed on the State through the awarding of federal financial assistance to subrecipients. While real progress has been made to address federal subrecipient issues, concerns still exist. In September 2003, Finance and Management issued Bulletin 5, Single Audit Policy for Subgrants. When fully implemented, Bulletin 5 is intended to enhance the State's compliance with federal grant requirements. However, similar attention has not been given to State-sponsored grants.

Based on the work performed during the audit, we have concluded the following:

- The State does not have policies or procedures to assist Departments in developing tools for monitoring a State subrecipient during the award period. As a result, many Departments do not have a mechanism in place to monitor subrecipients to ensure that the awarded funds are being spent in accordance with the written grant agreement.*
- The State does not have a system in place to help Departments identify when a subrecipient arrangement is created. As a result, many Departments are unaware of the fact that they have even entered into subrecipient relationships and are therefore not monitoring the funds that are awarded. As there are no guidelines, there is no consistent manner in which subrecipient awards are monitored.*

The State should evaluate its policies, procedures and controls over the monitoring of State grant funds awarded to subrecipients. This monitoring can be accomplished in a variety of ways, including program audits, site visits, or independent third party audits or reviews.

Absence of Linkage Between Authorization and Expenditure

The Department of Finance and Management continues to present its budgetary results on a cash-received and modified-cash paid basis. (In addition to cash paid, the State accrues certain expenditures on a budgetary basis.) The compilation of the budget numbers continues to be a manual process and the relationship between the budget in VISION, the State's centralized accounting system, and the authorizations passed by the Legislature is not clearly delineated. There continues to be little accountability within the State to match services provided to the proper fiscal year. While some invoices that have been entered into the VISION system have been accrued for, the State does not fully use the encumbrance process to restrict budgetary spending. This can lead to manipulation of the budgetary process by either: 1) holding invoices at year end and paying them out of the next year's budget thereby causing a mismatch between when a service is budgeted and when it is actually paid for; or 2) accelerating the payment of invoices to an earlier fiscal year to expend any remaining appropriation before a year closes. Both situations, if left unattended, can result in budgetary manipulation that will not be detected by State employees.

Manual and Complex Reconciliation Process

The preparation of the State's financial statements requires the coordination of departments and agencies throughout the State. While the Department of Finance and Management has made significant improvements in the underlying processes, continued effort and vigilance are required.

The State's accounting process is very decentralized and relies heavily on the individual departments and agencies to properly and accurately record activity on a timely basis. However, the Department of Finance and Management and the State do not have effective controls in place to ensure that the departments and agencies are discharging their financial accounting and reporting responsibilities. While the Department of Finance and Management is primarily responsible for preparing the State's financial statements, there are few controls in place over the financial reporting process to ensure information in the financial statements is analyzed or accurate. Existing controls are not sufficient to provide for:

- The effective oversight of departments/agencies that record financial activity to ensure they are using and reconciling departmental records to VISION. Since the Department of Finance and Management has not required all departments to use VISION, the reconciliation process is a critical control. Procedures should be in place to verify departments continue to reconcile the underlying financial information on a periodic basis.

- Automated compilation of the financial statement data and subsequent analysis of the information. A substantial amount of data needed to prepare the State's financial statements is still compiled manually.

In addition to the manual process used to compile the financial statements, the compilation of federal accounts receivable and the Schedule of Expenditures of Federal Awards is a long manual process subject to error. Moreover, much of the complex compilation rests on a single individual within the Department of Finance and Management, posing the risk of a Single Point of Failure should that individual become unavailable.

Policies, procedures, and controls should be in place to clearly specify the expectations on the part of Finance and Management with respect to ongoing financial reporting. This should include the commitment on the part of departments and agencies to perform periodic reconciliation of VISION to supporting documentation and procedures to verify compliance.

A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relation to the basic financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our joint consideration of internal control over financial reporting would not necessarily disclose all matters in internal control that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses. Of the reportable conditions described above, all are considered material weaknesses.

Although not considered to be a material weakness, we noted the following additional reportable condition:

Revenue Recognition

The preparation of the State's financial statements requires the use of assumptions and accruals to determine revenue and expense for the year. Policies, procedures, and controls have been placed in operation to ensure all material amounts are properly and accurately recorded in the appropriate financial reporting period. At the Tax Department, these policies and procedures are incorporated into the year-end closing processes. However, during the 2004 year-end closing the following errors and misstatements were noted:

- The State's accounting policy specifies that cash received in the 60-day period following year-end related to tax liabilities for the prior year be recorded as accrued revenue. During 2004 subsequent cash receipts related to personal income tax liabilities at June 30, 2004 were not recorded. This required an adjustment in the amount of \$3.2 million to properly state revenue.*
- The Legislature enacted a change as of July 1, 2004 in the allocation of tax revenue generated through the telecommunications sales and use tax. The new*

allocation places two-thirds of the revenue into the General Fund and one-third into the Education Fund. This change was not properly recorded by the State. This required an adjustment of approximately \$1 million to properly record revenue.

The above lack of attention placed on adherence to the policies and procedures is a concern. We strongly encourage the Tax Department to ensure all employees involved in the year-end closing process fully understand the policies and procedures related to the accumulation of information necessary to prepare complete and accurate financial statements. Procedures should be put in place to ensure that strict adherence to these policies is maintained.

We also noted other matters involving the design and operation of internal control over financial reporting which will be reported to management of the State in a separate report dated March 31, 2005.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the State of Vermont's basic financial statements referred to above are free of material misstatement, the State Auditor and KPMG LLP performed tests of the State's compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of the audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

This report is intended solely for the information and use of the Speaker of the House of Representatives, the President Pro-Tempore of the Senate, the Governor, management, the cognizant Federal agency, the Office of Inspector General and federal awarding agencies and is not intended to be and should not be used by anyone other than these specified parties.



Randolph D. Brock
State Auditor



KPMG LLP

March 31, 2005

Administration's Response to Auditor's Report on Internal Control Over Financial Reporting and Compliance and Other Matters

Listed below are the responses by the Administration to the material weaknesses and reportable condition contained in the *Report on Internal Control Over Financial Reporting and Compliance and Other Matters*.

Agency of Transportation Capitalization Issues

Condition Found

The preparation of financial statements in accordance with accounting principles generally accepted in the United States of America requires governmental entities to record and report capital assets. Capital assets include infrastructure assets such as roads and bridges. The assumptions underlying the capitalization of capital assets require that management establish policies, procedures and controls to record projects meeting its capitalization policy.

During 2003, management at the Agency of Transportation (AOT) reported its investment in infrastructure. During the preparation of the 2004 financial statements, management at AOT determined that its capitalization policy was not consistently applied. Specifically, management at AOT determined the following:

- A number of infrastructure projects were recorded as either capital assets or work in process at June 30, 2003. Additional costs were added to the projects during fiscal 2004. Management subsequently determined that ownership of these projects did not vest with the State of Vermont. Rather, these projects are owned by local municipalities throughout the State. As a result of this error, the 2004 financial statements were restated to remove approximately \$92 million of projects owned by the local municipalities.
- Concurrent with AOT's more thorough review of open construction projects, management determined that certain prior year infrastructure expenditures were not capitalized in accordance with the State's accounting policy. This required a restatement of the 2004 financial statements to capitalize approximately \$94 million of such expenditures.

The failure to consistently apply its capitalization policy and to ensure the accuracy of the information required to prepare complete and accurate financial statements constitutes a material weakness. Management should ensure its capitalization policy is consistently applied. This may require an evaluation of the front-end processes and controls in place to establish projects in the accounting system. Appropriate consideration should be given to ensure personnel with the requisite skills and knowledge of both project management and accounting are involved.

Administration Response

The recently-appointed Secretary of the Agency of Transportation recognizes the importance of appropriate and accurate application of financial accounting standards, including capitalization of capital assets. Both the Secretary and her newly-appointed Director of Finance and Administration have significant accounting and management experience. This will be brought to bear in ensuring that a sound internal control structure is in place. Specifically, the material weakness cited will be addressed by June 30, 2005, by undertaking several actions, including:

Assessing staff's skill and capabilities

Organizing and staffing relevant functions appropriately

Analyzing the capitalization policy and process

Designing any indicated process improvements

Developing or updating policies and procedures

Implementing new processes

Monitoring for compliance

Subrecipient Monitoring

Condition Found

In accordance with OMB Circular A-133, the State is required to adhere to laws and regulations pertaining to federal financial assistance programs administered by the State. While these same requirements are not mandatory for the proper control over State-funded grants, sound fiscal management would indicate that policies, procedures, and controls should be in place to ensure the expenditure of State funds are in accordance with State laws and regulations. Once a subrecipient relationship is created, the State has a responsibility to ensure that the subrecipient is made aware that they have been awarded State funds through a grant agreement and to determine whether or not the subrecipient has spent the awarded funds in accordance with State regulations by implementing and performing procedures to monitor the grant activities of the subrecipient. Through the results of procedures performed during the audit of the financial statements, we have determined that adequate procedures to ensure that the appropriate use of State pass-through funds is monitored do not exist. These requirements are similar to the requirements imposed on the State through the awarding of federal financial assistance to subrecipients. While real progress has been made to address federal subrecipient issues, concerns still exist. In September 2003, Finance and Management issued Bulletin 5, *Single Audit Policy for Subgrants*. When fully implemented, Bulletin 5 is intended to enhance the State's compliance with federal grant requirements. However, similar attention has not been given to State-sponsored grants.

Based on the work performed during the audit, we have concluded the following:

1. The State does not have policies or procedures to assist Departments in developing tools for monitoring a State subrecipient during the award period. As a result, many Departments do not have a mechanism in place to monitor subrecipients to ensure that the awarded funds are being spent in accordance with the written grant agreement.
2. The State does not have a system in place to help Departments identify when a subrecipient arrangement is created. As a result, many Departments are unaware of the fact that they have even entered into subrecipient relationships and are therefore not monitoring the funds that are awarded. As there are no guidelines, there is no consistent manner in which subrecipient awards are monitored.

The State should evaluate its policies, procedures and controls over the monitoring of State grant funds awarded to subrecipients. This monitoring can be accomplished in a variety of ways, including program audits, site visits, or independent third party audits or reviews.

Administration Response

We appreciate the Auditor's recognition that real progress has been made to address Federal subrecipient issues. We, like the Auditor, have concerns because this is still in the implementation stage. When fully implemented in State Fiscal Year 2006, we expect to be in full compliance with Federal grant requirements. However, to be in full compliance, we will need to ensure that there is adherence to Bulletin 5, and this will require follow-up with Departments.

We agree with the recommendation to establish policies, procedures and controls for State funded grants. The Commissioner of Finance & Management will establish statewide guidelines for granting State funds by June 30, 2006.

Absence of Linkage Between Authorization and Expenditure

Condition Found

The Department of Finance and Management continues to present its budgetary results on a cash-received and modified-cash paid basis. (In addition to cash paid, the State accrues certain expenditures on a budgetary basis.) The compilation of the budget numbers continues to be a manual process and the relationship between the budget in VISION, the state's centralized accounting system, and the authorizations passed by the Legislature is not clearly delineated. There continues to be little accountability within the State to match services provided to the proper fiscal year. While some invoices that have been entered into the VISION system have been accrued for, the State does not fully use the encumbrance process to restrict budgetary spending. This can lead to manipulation of the budgetary process by either: 1) holding invoices at year end and paying them out of the next year's budget thereby causing a mismatch between when a service is budgeted and when it is actually paid for; or 2) accelerating the payment of invoices to an earlier fiscal year to expend any remaining appropriation before a year closes. Both situations, if left unattended, can result in budgetary manipulation that will not be detected by State employees.

Administration Response

We agree that the compilation of the budget numbers continues to be a manual process. During the VISION upgrade, scheduled for completion during the fall of 2005, the Department of Finance and Management will evaluate the possibility of automating the generation of Budget to Actual Schedules.

The presentation of the State's Budget to Actual schedules are in accordance with Generally Accepted Accounting Principles. GASB's Codification of Governmental Accounting and Financial Reporting Standards, Section 1700.115 specifically states that the scope and method of state and local budgetary practices are outside the scope of financial reporting standards. Section 1700.116 states that the basis on which the budget is prepared establishes the basis on which the accounts are usually maintained and the budgetary reports must be prepared.

Given the above, we agree that the relationship between the budget in VISION, the state's centralized accounting system, and the authorizations passed by the Legislature is not clearly delineated. The Commissioner of Finance & Management will confer with the chairs of the House and Senate Appropriations Committees, by June 30, 2005, to gauge

Legislative intent regarding appropriations and costs in regards to the Budget to Actual Schedule presentations. Depending upon the outcome of this discussion, the Commissioner of Finance & Management will recommend legislation or establish policy to resolve this issue by June 30, 2006.

We agree that the State does not use the encumbrance system for all liabilities, and that this system should be used when it is determined to be cost effective.

Manual and Complex Reconciliation Process

Condition Found

The preparation of the State's financial statements requires the coordination of departments and agencies throughout the State. While the Department of Finance and Management has made significant improvements in the underlying processes, continued effort and vigilance are required.

The State's accounting process is very decentralized and relies heavily on the individual departments and agencies to properly and accurately record activity on a timely basis. However, the Department of Finance and Management and the State do not have effective controls in place to ensure that the departments and agencies are discharging their financial accounting and reporting responsibilities. While the Department of Finance and Management is primarily responsible for preparing the State's financial statements, there are few controls in place over the financial reporting process to ensure information in the financial statements is analyzed or accurate. Existing controls are not sufficient to provide for:

- The effective oversight of departments/agencies that record financial activity to ensure they are using and reconciling departmental records to VISION. Since the Department of Finance and Management has not required all departments to use VISION, the reconciliation process is a critical control. Procedures should be in place to verify departments continue to reconcile the underlying financial information on a periodic basis.
- Automated compilation of the financial statement data and subsequent analysis of the information. A substantial amount of data needed to prepare the State's financial statements is still compiled manually.

In addition to the manual process used to compile the financial statements, the compilation of federal accounts receivables and the Schedule of Expenditures of Federal Awards is a long manual process subject to errors. Moreover, much of the complex compilation rests on a single individual within the Department of Finance and Management, posing the risk of a Single Point of Failure should that individual become unavailable.

Policies, procedures, and controls should be in place to clearly specify the expectations on the part of Finance and Management with respect to ongoing financial reporting. This should include the commitment on the part of departments and agencies to perform periodic reconciliation of VISION to supporting documentation and procedures to verify compliance.

Administration Response

We appreciate the Auditor's acknowledgement that significant improvements in the underlying process have been made, and concur that continued effort and vigilance is required. We further agree that policies, procedures and controls should be in place to clearly specify the expectations on the part of Finance and Management with respect to ongoing financial reporting.

Based on information gathered during the next six months by our Operations Section, the Department of Finance and Management will issue its first report on best practices and minimum standards of control containing requirements to be implemented statewide by October 31, 2005. This is to include implementing new or revised controls over the financial reporting process to ensure information in the financial statements is analyzed, accurate and submitted on a timely basis.

The Department of Finance and Management is in the process of performing a technical upgrade to the VISION financial accounting system. This upgrade combined with the subsequent implementation of Time and Labor and the Projects Modules are the major steps required to fully transition major departments such as VTRANS and Employment and Training to VISION. This transition will eliminate the need for time consuming and costly reconciliations to secondary accounting systems. The VISION financial upgrade will be completed by November 30, 2005. The implementation of the Time and Labor module will commence immediately following the VISION financials upgrade and will be completed by August 31, 2006. The Projects Module implementation schedule has not been fully defined as of yet, but it is expected to commence soon after the completion of the Time and Labor implementation.

Reconciliations between secondary systems and VISION are required by the Department of Finance and Management and will be mandated in the State's monthly closing instructions.

The Financial Reporting Section is working toward entering adjustments into VISION so it can be used to directly generate the financial statements for the fiscal year 2006 Comprehensive Annual Financial Report. We do acknowledge that we have a Single Point of Failure and that more needs to be done to ensure information is analyzed and accurate. During fiscal year 2005, the Commissioner of Finance & Management further enhanced resources in the Financial Reporting Section to address these very important issues and our vulnerability noted by the Auditor. The Financial Reporting Section is cross training its staff in our financial reporting processes to ensure more than one individual can perform each of the Section's responsibilities.

Revenue Recognition

Condition Found

The preparation of the State's financial statements requires the use of assumptions and accruals to determine revenue and expense for the year. Policies, procedures, and controls have been placed in operation to ensure all material amounts are properly and accurately recorded in the appropriate financial reporting period. At the Tax Department, these policies and procedures are incorporated into year-end closing processes. However, during the 2004 year-end closing the following errors and misstatements were noted:

- The State's accounting policy specifies that cash received in the 60-day period following year-end related to tax liabilities for the prior year be recorded as accrued revenue. During 2004 subsequent cash receipts related to personal income tax liabilities at June 30, 2004 were not recorded. This required an adjustment in the amount of \$3.2 million to properly state revenue.
- The Legislature enacted a change as of July 1, 2004 in the allocation of tax revenue generated through the telecommunications sales and use tax. The new allocation places two-thirds of the revenue into the General Fund and one-third into the Education Fund. This change was not properly recorded by the State. This required an adjustment of approximately \$1 million to properly record revenue.

The above lack of attention placed on adherence to the policies and procedures is a concern. We strongly encourage the Tax Department to ensure all employees involved in the year-end closing process fully understand the policies and procedures related to the accumulation of information necessary to prepare complete and accurate financial statements. Procedures should be put in place to ensure strict adherence to these policies is maintained.

Administration Response

The Tax Department concurs with the adjustments noted above.

The Business Office staff has duly noted these adjustments in their workplan for preparation of all future Accounts Receivable Worksheets (form AAF-17). In addition, they requested and received a detailed, audited report of personal income tax accruals for July and August and this report will become an on-going part of their AAF-17 workpapers. Finally, the AAF-17 workplan has been updated to include not only an examination of the date accrued revenues are "earned", but also any revenue allocation changes in effect on the day accrued revenues are "received".

Administration's Response to 2004 Single Audit Findings

The findings listed below were taken from the June 30, 2004 Single Audit Report. Finding numbers correspond to the finding numbers used in the Single Audit Report. All of these findings are considered to be material weaknesses.

Finding 2004-6

Finance and Management

All Federal Programs in which the State Passes-Through Funds

Requirement

A pass-through entity shall perform the following for federal awards it makes: (1) Identify federal awards made by informing each subrecipient of CFDA title, award name and number, award year, if the award is R&D, and name of federal agency; (2) Advise subrecipients of requirements imposed on them by federal laws, regulations, and the provisions of contracts or grant agreements as well as any supplemental requirements imposed by the pass-through entity; (3) Monitor the activities of subrecipients as necessary to ensure that federal awards are used for authorized purposes in compliance with laws, regulations, and the provisions of contracts or grant agreements and that performance goals are achieved; (4) ensure that subrecipients expending \$300,000 or more in federal awards during the subrecipient's fiscal year have met the audit requirements of this part for that fiscal year; (5) Issue a management decision on audit findings within six months after receipt of the subrecipient's audit report and ensure that the subrecipient takes appropriate and timely corrective action; (6) Consider whether subrecipient audits necessitate adjustment of the pass-through entity's own records; and (7) Require each subrecipient to permit the pass-through entity and auditors to have access to the records and financial statements as necessary for the pass-through entity to comply with this part. (OMB Circular A-133.400(d))

Finding

In order to help achieve the objects of various federal award programs, the State of Vermont grants funds to third party subrecipients to carry out specific duties as allowed under federal regulations. Once a subrecipient relationship is created, the State has a responsibility to ensure that the subrecipient is made aware that they have been awarded federal funds through a grant agreement and to determine whether or not the subrecipient has spent the awarded funds in accordance with federal regulations by implementing and performing procedures to monitor the grant activities of the subrecipient. During our testwork over subrecipient monitoring throughout the State, we noted the following:

1. The State of Vermont does not have a system in place to help departments identify what a subrecipient is. As a result, many departments are unaware of the fact that they have even entered into subrecipient relationships and are therefore not properly monitoring the funds that are awarded as required by OMB. As there are no guidelines, subrecipient grant agreements do not contain the proper identifying information as required by OMB and the subrecipient is unaware that they have been awarded federal funds.

Finding 2004 – 6, Continued

2. The State of Vermont does not have a system in place to help departments track subrecipient grant payments. As a result, departments' are unaware that a single subrecipient may be receiving multiple awards from different State departments. As a result, subrecipient audit reports are not always obtained. This information would assist departments with meeting the monitoring requirement to obtain, review and issue management decisions concerning subrecipient audit reports. It would also eliminate any duplicate work performed across the State concerning the review of subrecipient audit reports as currently multiple departments are reviewing and following up on the same audit reports on an annual basis.
3. There are no policies and procedures in place to assist departments in the review of subrecipient audit reports. As a result, the review of subrecipient audit reports for types of opinions, compliance issues, internal control issues and agreement of financial data are not always performed.
4. The State of Vermont does not have policies or procedures to assist departments in developing subrecipient monitoring tools for monitoring a subrecipient during the award period. As a result, many departments do not have a mechanism in place to monitor subrecipients to ensure that the awarded funds are being spent in accordance with the written grant agreement. Furthermore, subrecipients receiving less than \$300,000 in assistance are frequently not monitored since they fall below the required audit threshold.

The lack of systems in place to effectively track and monitor subrecipients directly impacts the State's ability to ensure that federal awards that are passed through to grantees are used for allowable purposes under the federal award.

This finding is considered to be a material weakness.

Questioned Costs

Not determinable.

Recommendation

We recommend that the department implement the necessary procedures to ensure that all subrecipient grant payments are identifiable within the financial accounting system and are monitored in accordance with the above stated requirements.

Finding 2004-6, Continued

Management's Response

Steps to Correct:

On September 5, 2003, the Secretary of Administration issued Bulletin #5 entitled "Single Audit Policy for Sub-grants – Compliance with OMB Circular A-133". The purpose of this bulletin was to establish the State of Vermont's basic requirements for managing subrecipient grants. This bulletin outlines the process to be followed by departments involved with granting funds to subrecipients, including providing definitions of subrecipient versus vendor. It describes what information must be provided to subrecipients at the time a grant is made, and provides a standard grant document for departments' use in drafting grant awards, to ensure all requirements are met. This bulletin also lists the grantor's and grantee's responsibilities in regards to recordkeeping, monitoring, and audit. The bulletin also requires the Department of Finance and Management to establish a Primary Pass-Through entity for those sub-grantees receiving grants from multiple State Departments. The role of the Primary Pass-Through Entity is to coordinate the review of audits and to follow up with the sub-grantee as needed. Section XI of the policy provides guidelines for pass-through entities to use when reviewing sub-grantees that do and do not require audits. For those grantees that do require an audit, an audit review checklist is available as a supplement to Bulletin 5. This checklist provides a detailed guide for primary pass-through entities to use when reviewing and audit report.

In addition to the policy, a Subrecipient Grant Tracking database was implemented to allow the State to track all federal grants awarded to subrecipients from all grantors in the State. Sub-grantees are required to submit a Certification of Audit Requirement form to the Department of Finance and Management at the end of their fiscal year, signifying whether or not an audit is required. If an audit is not required, they are also required to submit the Schedule of Federal Expenditures, which details all expenditures, by federal CFDA number. If an audit is required, they are required to submit a copy of the audit to their designated Primary Pass-Through Entity as soon as it is completed, but within 9 months of their year-end. The Primary Pass-Through Entity is required to review the audit and follow up on any findings. Documentation of this review is to be made in the VISION Subrecipient Grant Tracking system as soon as it is complete.

This policy became effective during state fiscal year 2004 and all grants written to subrecipients since September 1, 2003 are required to be entered into the VISION system. As of February 15, 2005, approximately 2,600 grants to over 800 subrecipients have been recorded in VISION. The Department of Finance and Management has designated an employee to review subrecipient data in the VISION system, to assign Primary Pass-Through Entities, and to assist departments as needed with the implementation of this policy. To date, the Dept. of Finance and Management has received the required forms from and designated a primary pass-through entity for approximately 400 subrecipients. Of those, approximately 100 require a single audit. Review of these audits is just beginning and will be ongoing since grantees with a June 2004 fiscal year-end are required to submit their single audit reports by March 31, 2005. In addition, a new version of the VISION subrecipient system is scheduled to go live by February 28, 2005.

Finding 2004-6, Continued

This new version enhances the monitoring functionality of the system allowing for more complete documentation of subrecipient review. The Dept. of Finance and Management now believes that the State of Vermont now complies with OMB Circular A-133 and the first full year of subrecipient review should be complete during State fiscal year 2006.

Estimated Completion Date: Fiscal year 2006.

Contact Person: Bradley Ferland, Director of Financial Operations, Department of Finance & Management - 802-828 2336.

Finding 2004-7

Finance and Management

All Federal Programs

Requirement

The auditee shall: (a) Identify, in its accounts, all Federal awards received and expended and the Federal programs under which they were received. Federal program and award identification shall include, as applicable, the CFDA title and number, award number and year, name of the Federal agency, and name of the pass-through entity; and (d) Prepare appropriate financial statements, including the schedule of expenditures of Federal awards in accordance with OMB Circular A-133 section .310.

Finding

During the our audit of the State of Vermont's federal expenditures, we noted that the State does not have a system in place for compiling the federal expenditure data needed to prepare the Schedule of Expenditures of Federal Awards (the "Schedule"). During our audit of the State's federal expenditures for the period ending June 30, 2004, we noted that the VISION system does not identify the following:

1. CFDA title and number;
2. Award number and year;
3. Name of Federal Agency; and
4. Name of the pass-through entity.

In addition, the VISION system does not capture the cost associated with non-cash expenditures received as federal awards, including immunization grants and food commodities.

This finding is considered to be a material weakness.

Questioned Costs

Not determinable.

Recommendation

We recommend that Finance and Management implement the necessary action to ensure that all federal awards are properly accounted for and identified within the financial accounting system in order to ensure that all expenditures are properly reported within the Schedule of Expenditures of Federal Awards and that the Schedule is supported or reconciled to the State's accounting system.

Finding 2004-7, Continued

Management's Response

Steps to Correct:

In July of 2001 when the State of Vermont implemented VISION, it was Finance and Management's expectation that all departments would use the functionality available in VISION to record and track federal awards and the related expenditure of those awards. The functionality provided in VISION allows departments to track awards (funding sources) based on the Federal Aid Agency, the pass-through entity, the funding year and the CFDA number. Additionally, VISION allows departments to tie expenditures to these federal awards through the use of the Project/Grant chart-field. Full implementation of this functionality would allow for an accurate reconciliation of federal expenditures to financial statement amounts. It was not until the end of FY2002 that the Department of Finance and Management became aware that certain departments were not using this functionality to track the required information. By analyzing the information in VISION, Finance and Management has concluded that the functionality is working as designed for those departments that did use it as instructed. In fiscal year 2005 it is the goal of Finance and Management to continue obtaining a better understanding of why some departments chose not to use this functionality and where possible, move them toward doing so as soon as possible. In the meantime, the compilation of the data for the Schedule of Federal Awards will continue to be on a manual basis.

Scheduled Completion Date: Fiscal year 2006.

Contact Person: Bradley Ferland, Director of Financial Operations, Department of Finance & Management 802-828-2336.

Finding 2004 – 8

Agency of Transportation

Federal Transit Administration Cluster:

Capital Investment Grants - Capital Grants (CFDA #20.500)

Formula Grants – Urbanized Area Formula Grants (CFDA #20.507)

Requirement

The Financial Status Report (FSR) (SF-269 (OMB No. 0348-0039) or SF-269A (OMB No. 0348-0038)). Recipients use the FSR to report the status of funds for all non-construction projects and for construction projects when the FSR is required in lieu of the SF-271.

Condition Found

During our testwork over federal reporting we noted that the data used to prepare the federal reports is obtained directly from the STARS system (the Agency's federally approved system for tracking project costs), which has not been reconciled to the VISION system (the State's centralized accounting system) in a timely manner, and therefore we were unable to test the completeness of the data.

This appears to be a systemic deficiency that could result in expenditures being reported that are not maintained within the statewide financial accounting system that could affect the credibility of the data reported on the SF-269 report.

This finding is considered to be a material weakness.

Questioned Costs

Not determinable.

Recommendation

We recommend that the Agency implement the necessary policies and procedures to ensure the required reports are accurately stated and are in accordance with federal requirements.

Finding 2004 – 8, Continued

Management's Response

Steps to Correct:

The 2004 reconciliation between STARS and VISION was completed in November 2004. Adjusting entries have been entered in both systems which will help ensure that the federal reports are accurate. Our goal is to ensure that all reconciliations are complete and adjustments are entered in both systems before the subsequent month closes. Expenditure reconciliations between STARS and VISION for FY 05 as of March 2, 2005 are current with January 05 fiscal month activity.

Scheduled Completion Date: We consider the corrective action to be completed.

Contact Person: Raylene Jacobs, Chief Financial Officer, (802) 828-2834.

Finding 2004 – 10

Agency of Transportation

Formula Grants for Other Than Urbanized Areas (CFDA #20.509)

Requirement

Financial Status Report (FSR) (SF-269 (OMB No. 0348-0039) or SF-269A (OMB No. 0348-0038)). Recipients use the FSR to report the status of funds for all non-construction projects and for construction projects when the FSR is required in lieu of the SF-271.

Condition Found

During our testwork over federal reporting, we noted that the data used to prepare the federal reports is obtained directly from the STARS system (the Agency's federally approved system for tracking project costs), which has not been reconciled to the VISION system (the State's centralized accounting system) in a timely manner, and therefore we were unable to test the completeness of the data.

This appears to be a systemic deficiency that could result in expenditures being reported that are not maintained within the Statewide financial accounting system that could affect the credibility of the data reported on the SF-269 report.

This finding is considered to be a material weakness.

Questioned Costs

Not determinable.

Recommendation

We recommend that the Agency implement the necessary policies and procedures to ensure the required reports are accurately stated and are in accordance with federal requirements.

Finding 2004 – 10, Continued

Management's Response

Steps to Correct:

The 2004 reconciliation between STARS and VISION was completed in November 2004. Adjusting entries have been entered in both systems which will help ensure that the federal reports are accurate. Our goal is to ensure that all reconciliations are complete and adjustments are entered in both systems before the subsequent month closes. Expenditure reconciliations between STARS and VISION for FY 05 as of March 2, 2005 are current with January 05 fiscal month activity.

Scheduled Completion Date: We consider the corrective action to be completed.

Contact Person: Raylene Jacobs, Chief Financial Officer, (802) 828-2834.

Finding 2004 – 13

Agency of Human Services

State Administrative Matching Grants for Food Stamp Program (CFDA #10.561) Temporary Assistance for Needy Families (CFDA #93.558)

Requirement

A pass-through entity is responsible for:

- *Award Identification* - At the time of the award, identifying to the subrecipient the Federal award information (e.g., CFDA title and number, award name, name of Federal agency) and applicable compliance requirements.
- *During-the-Award Monitoring* - Monitoring the subrecipient's use of Federal awards through site visits or other means to provide reasonable assurance that the subrecipient administers Federal awards in compliance with laws, regulations, and the provisions of contracts or grant agreements and that performance goals are achieved.
- *Subrecipient Audits* - Ensuring required audits are completed within nine months of the end of the subrecipient's audit period, issuing a management decision on audit findings within six months after receipt of the subrecipient's audit report, and ensuring that the subrecipient takes timely and appropriate corrective action on all audit findings. In cases of continued inability or unwillingness of a subrecipient to have the required audits, the pass-through entity shall take appropriate action using sanctions.
- *Pass-Through Entity Impact* - Evaluating the impact of subrecipient activities on the pass-through entity's ability to comply with applicable Federal regulations.

Condition Found

The Department has approximately sixty-five different agencies that provide various Reach Up services in connection with the Welfare-to-Work initiative. The agencies provide Reach Up services for both Temporary Assistance for Needy Families (TANF) and Food Stamp recipients and therefore most agencies receive federal funding under both programs to help pay for their activities.

During our testwork over the subrecipient monitoring process, we noted the following:

- A. The Department performs periodic site visits to ensure that all subrecipients are providing services in accordance with the signed grant agreement. We noted that a site visit was not conducted for one out of the fifteen grants selected.

Finding 2004 – 13, Continued

- B. For eleven of the fifteen grants selected for testwork, we noted that the Department did not obtain or review the subrecipient's audit reports as required under Circular OMB A-133.
- C. One out of the fifteen grants selected for testwork was entered into with another Department within the same Agency. During our testwork, we noted that the Department did not monitor the receiving Department to ensure the services performed were in accordance with the agreement that was entered into.

The above noted compliance deficiencies appear to be systemic. Ineffective policies and procedures for monitoring subrecipient grants impacts the Department's ability to ensure that subrecipients are utilizing the federal funding awarded for allowable activities.

This finding is considered to be a material weakness.

Questioned Costs

None noted.

Recommendation

We recommend that the Department review its policies and procedures to ensure that a uniform system is in place to monitor all subrecipients. Such procedures should include obtaining and reviewing financial statements and A-133 audit reports on a timely basis.

Management's Response

Steps to Correct:

The Agency of Human Resources has been authorized to reorganize financial operations. This reorganization began this year and will provide additional resources to address the subrecipient monitoring issues. The Agency will obtain and review financial statements and A-133 Audit reports for all subrecipients

Scheduled Completion Date: June 30, 2006.

Contact Person: David Cohen, Department of Children and Families, (802) 241-1270.

Finding 2004 – 16

Agency of Human Services

Centers for Disease Control and Prevention - Investigations and Technical Assistance (CFDA #93.283)

Requirement

Matching or cost sharing includes requirements to provide contributions (usually non-Federal) of a specified amount or percentage to match Federal awards. Matching may be in the form of allowable costs incurred or in-kind contributions (including third-party in kind contributions).

The specific requirements for matching, level of effort, and earmarking are unique to each Federal program and are found in the laws, regulations, and the provisions of contract or grant agreements pertaining to the program.

However, for matching, the A-102 Common Rule ('____.24) and OMB Circular A-110 ('____.23) provide detailed criteria for acceptable costs and contributions. The following is a list of the basic criteria for acceptable matching:

- Are verifiable from the non-Federal entity's records.
- Are not included as contributions for any other Federally-assisted project or program, unless specifically allowed by Federal program laws and regulations.
- Are necessary and reasonable for proper and efficient accomplishment of project or program objectives.
- Are allowed under the applicable cost principles.
- Are not paid by the Federal Government under another award, except where authorized by Federal statute to be allowable for cost sharing or matching.
- Are provided for in the approved budget when required by the Federal awarding agency.
- Conform to other applicable provisions of the A-102 Common Rule and OMB Circular A-110 and the laws, regulations, and provisions of contract or grant agreements applicable to the program.

Condition Found

The Department operates nine grants as part of the Centers for Disease Control and Prevention – Investigations and Technical Assistance. Of the four grants selected for testwork, the Tobacco Control Grant and the Cancer Prevention and Control Grant had matching requirements that needed to be met. During our testwork over the matching process, we noted the following:

Finding 2004 – 16, Continued

1. The Tobacco Control Grant has a one-to-one match requirement meaning that for each federal dollar spent the state must match one dollar in nonfederal expenditures. The Department meets its matching requirement through the use of allocated Tobacco Settlement Funds that are budgeted to the Department on an annual basis. At the end of the grant period, the program specialist prepares a spreadsheet that compares the total amount of Tobacco Settlement Funds expended for the year to the amount of federal funds expended for the Tobacco Control Grant to ensure that the necessary match has been met. During our review of the matching process, we noted that the Department does not report the match on the Financial Status Report that is filed on an annual basis. As such we could not determine what the actual match was that the Department would have included.
2. The Cancer Prevention and Control Grant has a three-to-one matching requirement, meaning that for every three federal dollars spent, the Department must spend one dollar. The Department meets its required match through a variety of external sources. During our testwork over the matching process, we noted the following:
 - A. The Department met \$382,964 of its matching requirement through contributed physician services for cancer screenings through the LadiesFirst Program. Under this program, the Department has agreed to reimburse the provider the Medicare “B” reimbursement rates. The provider agrees not to bill the patient for any additional amount. The portion that is left “unpaid” is considered to be a contributed service by the provider and is included by the Department in the calculation of its matching requirement. We selected thirty physician invoices that were utilized in the matching process and noted the following:

Six out of thirty invoices selected for testwork were for patients that had a private insurance carrier. The provider initially billed the private insurance carrier for the screening and then billed the Department for the remaining difference, resulting in a payment less than what the full Medicare “B” rate would have been. In these instances, the Department could not provide the explanation of benefits that was received and therefore we could not determine whether the Department had properly accounted for this match.

The Department requires that providers sign a provider agreement with the Cancer Prevention and Control program to authorize the program to utilize the unbilled expenses as contributed services towards the Department’s match requirement. Two out of thirty provider agreements could not be located and therefore we could not determine whether or not the provider had authorized the Department to utilize the unbilled expense as a contributed service.

One out of thirty invoices selected for testwork was not paid correctly based on the Medicare “B” rate. The Department paid \$636 and per the Medicare “B” rate schedule they should have paid \$582.

Finding 2004 – 16, Continued

- B. An additional \$97,708 of the required match was provided through the Cancer Registry Service. The Cancer Registry Service is a databank used by the Department to track medical and state-wide health trends concerning cancer hospitals are required to report incidence of cancer to the Cancer Registry as required by the Vermont Cancer Reporting Law. In 1998, the Department determined that the cost of each abstract reported by the hospital (with the abstract containing the cancer information) was \$41.42. Each year, the Department multiplies the total number of abstracts received by the rate of \$41.42 to determine the hospital's contributory service towards the Department's matching requirement. The number of abstracts is obtained from the Department's registry system, and can be uploaded to provide support the transaction total. During our testwork over these matching funds, the Department was unable to provide any documentation to support how the cost of \$41.42 was derived nor that the estimate had been reviewed to ensure that it was still valid for the year ending June 30, 2004. As a result, we are unable to determine the reasonableness of this matching source of funds.

The deficiencies noted above over the tracking of matching funds appear to be systemic. The lack of procedures in place for monitoring and reporting matching funds could result in the Department not providing the necessary matching funds to support the Federal funds expended and drawn down in a given year. The effect of not providing the proper matching funds is that Federal funds would be drawn down to soon, impacting the Department's compliance with cash management requirements.

This finding is considered to be a material weakness.

Questioned Costs

Not determinable.

Recommendation

We recommend that the Department implement the necessary policies and procedures to adequately monitor and reconcile the matching requirements of all grants to ensure compliance with federal requirements.

Management's Response

Steps to Correct:

- 1) The Department will report the required match expenditures on future Financial Status reports for the Tobacco Control grant. For the reporting period in question, our match expenditures would have been sufficient to meet federal requirements.

Finding 2004 – 16, Continued

Management's Response, Continued

2) A. In relation to the thirty physician invoices in the Cancer Prevention and Control program:

We agree that the explanation of benefits document (EOB) is missing for six out of thirty invoices. The Department has since changed its procedures. In the past, the EOB was generally sent to the business office with the invoice. Now the EOB is maintained in the program files, minimizing the chances of the EOB going astray.

We agree that two of the thirty agreements between providers and the Cancer Prevention and Control program could not be located. The Department has initiated plans to change its procedures for signing and filing of the agreements. When EDS takes over responsibility for processing payments, EDS will require that providers sign and return the agreement as part of the process of enrolling as an EDS provider. Under this arrangement, providers will have an incentive to complete the agreement since enrolling as an EDS provider is a requirement for obtaining payments.

The Department agrees that there is no documentation to support its payment of one invoice in an amount that was \$53.85 higher than the Medicare "B" rate.

B. The Department has updated the data and described the procedures used to determine the match available through reporting the cost of hospital abstracts. The procedure used was the one proposed as a corrective action in response to a similar finding in the FY03 audit. This was completed November 1, 2004, subsequent to the audit period. The current weighted average cost of abstracts is now reported as \$70.77 rather than \$41.42.

Scheduled Completion Date: June 30, 2005.

Contact Person: Patrick Burke, Federal Grants Manager, Department of Health, (802) 863-7257.

Finding 2004 – 18

Agency of Human Services

Centers for Disease Control and Prevention - Investigations and Technical Assistance (CFDA #93.283)

Requirement

To provide reasonable assurance that eligibility requirements are met based on specific criteria for determining the individuals can participate in the program and the amounts for which they qualify.

Condition Found

The Breast and Cervical Cancer Screening grant is a specialized program that is funded through the use of funds from the Centers for Disease Control and Prevention - Investigations and Technical Assistance program. The Breast and Cervical Cancer Screening grant agreement allows for the program to provide screenings for women who are among the lower income group. During our review of this process, we noted that the Department could not readily determine what portion of the Breast and Cervical Cancer Screening grant related to the screening and prevention costs associated with payments made for individuals who were participants in the program and as such we were identify unable to the dollar value associated with this requirement to determine if this requirement was direct and material. This appears to be a systemic compliance deficiency and could lead to ineligible participants receiving services under the program, resulting in unallowable costs charged to the program.

This finding is considered to be a material weakness.

Questioned Costs

Not Determinable.

Recommendation

We recommend that the Department implement the necessary policies and procedures to adequately monitor the screening and prevention costs of this grant to ensure only eligible participants receive services under the federal program.

Finding 2004 – 18, Continued

Management's Response

Steps to Correct:

We agree that it is not possible to determine the amount expended on a person-by-person basis. The VISION system is not designed to track expenditures by individual clients. Before the end of FY05, the Department intends to shift away from paying for screenings through the VISION system. Instead, the payments will be made by EDS on behalf of the Breast & Cervical Cancer Screening program. We hope that the EDS reporting system will allow us to track expenditures on a person-by-person basis.

Scheduled Completion Date: June 30, 2006.

Contact Person: Patrick Burke, Federal Grants Administrator, Department of Health, (802) 863-7257.

Finding 2004 – 19

Agency of Human Services

Centers for Disease Control and Prevention - Investigations and Technical Assistance (CFDA #93.283)

Requirement

A pass-through entity is responsible for:

- Identifying to the subrecipient the Federal award information (e.g., CFDA title and number, award name, name of Federal agency) and applicable compliance requirements.
- Monitoring the subrecipient's use of Federal awards through reporting, site visits, regular contact, or other means to provide reasonable assurance that the subrecipient administers Federal awards in compliance with laws, regulations, and the provisions of contracts or grant agreements and that performance goals are achieved.
- Ensuring that subrecipient's expending \$300,000 (\$500,000 for fiscal years ending after December 31, 2003 as provided in OMB Circular A-133, as revised) or more in Federal awards during the subrecipient's fiscal year have met the audit requirement of OMB Circular A-133 and that the required audits are completed within nine months of the end of the subrecipient's audit period, issuing a management decision on audit findings within six months after receipt of the subrecipient's audit report, and ensuring that the subrecipient takes timely and appropriate corrective action on all audit findings. In cases of continued inability or unwillingness of a subrecipient to have the required audits, the pass-through entity shall take appropriate action using sanctions.
- Evaluating the impact of subrecipient activities on the pass-through entity's ability to comply with applicable Federal regulations.

Condition Found

The Department grants funds to various organizations to support programs as designed by the Federal grant award. All subrecipients are required to sign a grant agreement that outlines what the funding is to be used for, the total amount of funds being awarded and specific program requirements that must be met, such as the submission of invoices, financial or programmatic reports. During our testwork over subrecipient monitoring, we selected twenty-five grantees and noted the following:

Finding 2004 – 19, Continued

- A. There were two instances out of twenty-five where there was not a formal grant agreement written up. This was a result of a transfer that occurred between another State Agency.
- B. There were four instances out of twenty-five where the activities approved under the grant agreement appeared to be more related to contract services than grant services.
- C. There was one instance out of twenty-five where the grant was improperly coded per the coding/cover sheet and the expenditures were charged to the wrong program that is included as part of the Centers for Disease Control and Prevention - Investigations and Technical Assistance.
- D. There were seven instances out of twenty-five where the grant award document did not contain the proper CFDA number for the current year but rather contained the CFDA number for the prior year. We noted that the award number included on the grant award document did represent the current year award number.
- E. There was one instance out of twenty-five where the coding/cover sheet did not contain proper approval.
- F. Included in the signed grant agreement is a requirement that subrecipients have an A-133 audit if they expend more than \$300,000 in federal funds. During our review of the subrecipient files we noted that audit reports were not obtained. Although the grant awards are typically below the \$300,000 threshold requiring an A-133 audit, the Department has no mechanism in place to determine whether the subrecipient received awards from other sources that would have required them to have a single audit.
- G. Various progress and year-end financial and programmatic reports are required to be submitted by the grantees. We noted that ten out of the twenty-five subrecipients did not submit the documentation as required by the grant award document and the Department did not follow-up regarding this documentation.
- H. Various progress and year-end financial and programmatic reports are required to be submitted by the grantees. During our review of the programs we noted that eight out of the twenty-five subrecipients did submit the documentation as required by the grant award document, and there was no formal documentation that the Department had reviewed or approved the reports that were received. In addition, some of the reports do not include documentation to determine whether the funds were spent on allowable activities. Overall, the Department does not appear to have sufficient mechanisms in place to ensure that awarded funds are spent on allowable activities in accordance with the grant agreements.

Finding 2004 – 19, Continued

The above instances appear to be systemic compliance deficiencies. The lack of procedures to ensure that subrecipient grants are properly monitored increases the risks that federal funding could be spent by the subrecipient on unapproved and unallowable activities.

This finding is considered to be a material weakness.

Questioned Costs

Not determinable.

Recommendation

We recommend that the Department review its existing subrecipient monitoring policies and procedures and implement the necessary measures to adequately monitor the funds to help ensure that all subrecipient expenditures are allowable and in compliance with federal regulations.

Management's Response

Steps to Correct:

- A. As MOU which cites the required A-133 information is standard procedure when making payment in support of another State Agency's program. This information was not included in the two payments referenced in the finding. At the time, the Department had only recently initiated this procedure; we expect that future payments will be accompanied by adequate information.
- B. Of the four grants noted which appear to more like contracts, two (#3631, 3531) were payments giving financial support of conferences largely designed, organized and implemented by the grantee, and a grant payment was probably appropriate. The other two (#3495, 3665) were not the usual type of support to a grantee, as noted in the finding. The Department intends to review alternatives other than grant payments in such situations.
- C. We agree that there was one instance where a grant payment was ultimately charged to a program other than that indicated on the coding sheet. However, the particular payment in question is eligible under both the original program indicated on the coding sheet and the program that was ultimately charged.
- D. We agree that there were instances where the CFDA number from the prior year was used incorrectly. We will now be more alert to changes in CFDA numbers. Prior to this event, there was virtually no situation in which the CFDA number had changed from one year to the next.

Finding 2004 – 19, Continued

Management's Response, Continued

- E. We agree that there was one instance of the “approval” section on the coding sheet not being filled out. The label of this section is misleading. The actual approval of the invoice for payment is done by a program person, but not in this section. This section allowed space for initials of the Accounts Payable supervisor, which was only intended to indicate that she has deemed the data entry to be correct, not that she had approved of the payment. We revised the coding form effective July 1, 2004 to make this approval process clearer. This section now reads: “A/P Sup Review for Data Entry.”
- F. We agree that the Department has no mechanisms in place to determine whether subrecipients receive funds from other entities that would put them over the threshold amount for A-133 audits. Aside from the question of whether A-133 requires us to take that action, or whether it simply requires us to give the grantee certain specified data and to review audits if they are submitted, the procedures in Vermont’s Bulletin 5 specify that the Finance Department has that responsibility for the State. For most of the period under audit, the Finance Department was not staffed to implement this function. They now have filled a position to implement those procedures.
- G. The Department agrees that lack of subgrantee financial and program reports is a problem. The Department initiated corrective action related to this finding in FY04. Policies and procedures were drafted to address the need to obtain reports from subrecipients, to follow up when the reports are not submitted and the need to document Health Department review of the reports when they are received. These new policies were developed with broad input from all divisions and were instituted in a half-day training session for all affected staff in May 2004. They were effective July 1, 2004, after the end of this audit period.
- H. The Department agrees that lack of documentation of review of subgrantee reports is a problem, as is the existence of reports that are unable to demonstrate that funds were spent on allowable activities. The Department has initiated a corrective action plan, as described above, and we expect to see improvement in FY05.

Scheduled Completion Date: June 30, 2005.

Contact Person: Patrick Burke, Federal Grants Administrator, Department of Health, (802) 863-7257.

Finding 2004 – 20

Agency of Human Services

Immunization Grants (CFDA #93.268)

Requirement

A pass-through entity is responsible for:

- Identifying to the subrecipient the Federal award information (e.g., CFDA title and number, award name, name of Federal agency) and applicable compliance requirements.
- Monitoring the subrecipient's use of Federal awards through reporting, site visits, regular contact, or other means to provide reasonable assurance that the subrecipient administers Federal awards in compliance with laws, regulations, and the provisions of contracts or grant agreements and that performance goals are achieved.
- Ensuring that subrecipient's expending \$300,000 (\$500,000 for fiscal years ending after December 31, 2003 as provided in OMB Circular A-133, as revised) or more in Federal awards during the subrecipient's fiscal year have met the audit requirement of OMB Circular A-133 and that the required audits are completed within nine months of the end of the subrecipient's audit period, issuing a management decision on audit findings within six months after receipt of the subrecipient's audit report, and ensuring that the subrecipient takes timely and appropriate corrective action on all audit findings. In cases of continued inability or unwillingness of a subrecipient to have the required audits, the pass-through entity shall take appropriate action using sanctions.
- Evaluating the impact of subrecipient activities on the pass-through entity's ability to comply with applicable Federal regulations.

Monitoring For-Profit Subrecipients

Significant portions for this program are passed through from the pass-through entity (usually the State) to for-profit subrecipients in the form of vaccine. Since OMB Circular A-133 does not apply to for-profit subrecipients, the pass-through entity is responsible for establishing requirements as necessary to ensure compliance by for-profit subrecipients (OMB Circular A-133 _____.210(e)) and for monitoring and reporting program performance by for-profit subrecipients (A-102 Common Rule '____.40(a)). The compliance requirements applicable to for-profit subrecipients under this program are:

- a. Eligibility requirements in "III.E.1 Eligibility for Individuals"

Finding 2004 – 20, Continued

- b. Control of vaccine in "III.N.1 Control, Accountability, and Safeguarding of Vaccine"
- c. Record keeping in "III.E.2 Record of Immunization"

Condition Found

The Department receives the majority of all requested vaccines under the Immunization Grant Program directly from the Centers for Disease Control (CDC) on an as needed basis. The vaccines are then distributed to a network of District Health Offices throughout the State of Vermont based on each District Office requesting the vaccine. The vaccines that are provided to the District Offices are then distributed to local health care providers that have enrolled in the Vaccines for Children Program (VFC). Once enrolled, the health care provider is required to submit a Vaccine Accountability Sheet to the District Office requesting the type and amount of each vaccine that is needed. Once received, the health care provider administers the vaccine directly to the patient. The Vaccine Accountability Sheets are provided to the Central Office, to update the inventory on hand for each District Office and Provider.

In order to ensure that the local health care provider and District Office is properly accounting for and administering the vaccines under the Immunization Grant Program, the Department conducts an on-site monitoring review of individual providers and District Offices. A questionnaire is completed that discusses areas such as the provider's storage of vaccine and who they are administering the vaccine to. In addition, the Department conducts a chart review to ensure that the provider is maintaining adequate records to track who the vaccines were administered to.

During our testwork over the provider monitoring process, we noted the following:

- A. The Department does not distinguish between for profit and non-profit health care providers. As a result, the Department has no mechanisms in place to determine which providers are having an audit performed in accordance with OMB Circular A-133. In addition, the Department does not request, receive or review any audited financial statements or single audit reports from any provider currently receiving vaccines under the Immunization Grant Program.
- B. Providers are required to report to the Department the dates in which vaccines were administered to patients during the prior month as well as the age category that the patient fell in when placing an order for vaccines with the District Office. While this data is collected, the Department has no mechanisms in place to determine whether or not the data submitted by the provider is correct and complete. In addition, per discussion with the Department, various providers often do not complete the form correctly and show all doses being administered to the same age group all on the same day.

Finding 2004 – 20, Continued

- C. The Department acts as the centralized depot for all vaccines for enrolled providers in the State of Vermont, in that those providers are also able to obtain all their required vaccines from the State of Vermont in addition to the VFC program. Vaccines are distributed to each provider based on lot number. The Department does not have controls in place to ensure that the vaccines that are distributed to providers under the VFC program were indeed administered to VFC eligible individuals.
- D. The Department conducts on-site reviews of providers during the year. At the end of the review, the Department prepares a written report that is sent to the providers to discuss the results of the on-site review and any corrective action that is required. Of the reviews selected for testwork, two of the twenty-one providers and four of the four district offices did not receive a written report.
- E. As part of the VFC program, there are certain eligibility requirements that must be met in order for an individual to receive a vaccine from a provider. The questionnaire that is utilized by the Department inquires whether or not the provider monitors VFC eligibility. The Department has not made this a requirement for providers to verify an individual's eligibility and has not routinely monitored this requirement. During our testwork over the monitoring process, we noted that the reviewer indicated for all twenty-one providers selected for testwork that the provider did not monitor for VFC eligibility. The Department did not require corrective action from the providers. For all four district offices selected for testwork, the reviewer indicated that the district offices screened for VFC eligibility, however the reviewer did not review any files to substantiate this claim.
- F. As part of the on-site review, the Department conducts a chart review of selected patients to ensure that the proper identifying information has been recorded in regards to the vaccine such as date administered and lot number. We noted for twelve of the fifteen providers, that the reviewer did not include the names of the children that were selected for the VFC eligibility review and/or the information did not contain enough to know what the reviewer had looked out during their file review (i.e. patient identifier, date of birth, vaccine product, date of administration, manufacture, lot #, vaccine administration initials, VIS publication date, and VFC screening). In addition, the reviewer did not include these issues identified in the written documentation of the site visit.
- G. As part of the on-site review, the Department conducts a chart review of selected patients to ensure that the proper identifying information has been recorded in regards to the vaccine such as date administered and lot number. We noted nine of the fifteen providers that the reviewer did include the children that were selected for the VFC eligibility review as evidence of either the child's full names or their initials. However, there were deficiencies found in the review of these files. For example: for all children reviewed, it was noted that the child was not screened for VFC eligibility by the provider. The reviewer did not include these issues identified in the in the written documentation of the site visit.

Finding 2004 – 20, Continued

- H. As a result of the Department's on-site reviews, several areas of non-compliance or concerns were noted on the questionnaire. Of the reviews selected for testwork, nine of the twenty-one provider site reviews had received a notice that they were lacking vaccine management protocols however, the Department did not request a corrective action plan.
- I. As a result of the Department's on-site reviews, one of the twenty-one provider site reviews noted that the provider had swapped privately supplied vaccines with the Department vaccines on hand. The provider had intentions of replacing these vaccines upon receipt of the private vaccines. The state did not know how to make the provider pay for the waste of over 100 vaccines that were administered for non-eligible children and as such asked that the provider indicated that these were wasted vaccines.
- J. As a result of the Department's on-site reviews, twenty of the twenty-one provider site reviewed noted that the practice does not have the necessary procedures in place for documenting immunization records, such as including the date and lot number of the vaccine administered. We noted that the chart review questions regarding the vaccine product, date administered, manufacture, lot number, name of person administering vaccine and the VIS publication date were often found to be missed. In most instances, it was the name of the person administering vaccine, manufacturer, lot number and the VIS publication date. The Department did not include these deficiencies on the eport issued to the provider.
- K. The Department requires the providers to submit Vaccine Accountability Sheets which details the number of Vaccines distributed (i.e. Hep B, Influenza, etc) by age, vaccine lot numbers, number of wasted vaccines, etc. Of the two months selected for testwork for each provider, one out of twenty-one provider Vaccine Accountability Sheets could not be located and per the VACMAN inventory tracking system this provider had accounted for their vaccines during that particular month. In addition, of the two months selected for testwork for each provider, one out of twenty-one provider Vaccine Accountability sheets did not agree to VACMAN inventory tracking system.

The above instances noted appear to be systemic compliance deficiencies. The lack of procedures in place to monitor providers increases the risk that the Department would not be able to identify if vaccines are being provided to ineligible children, resulting in an unallowable cost.

This finding is considered to be a material weakness.

Questioned Costs

Not determinable.

Finding 2004 – 20, Continued

Recommendations

We recommend that the Department implement the necessary policies and procedures to ensure that providers are monitored in accordance with federal requirements. This includes ensuring that all providers are properly submitting annual reports that are reviewed by the Department, properly documenting the results of on-site monitoring visits and issuing a management decision on the visits timely to the provider.

Management's Response

Steps to Correct:

- A. In response to a similar finding in last year's audit, the Department proposed "Check boxes will be added to enrollment forms for practices to self-identify as for profit or non-profit. The Department will request audits from providers as required." We acknowledge that we failed to take this action in time to change our practice in the period audited. We will take this corrective action this year.
- B. Providers are required to report to the Department the antigen administered and the patient age for all vaccines administered during the previous month. Additionally they are required to report their current inventory. This information must be submitted to District Office when placing a new order for vaccines. Any reporting discrepancies are resolved at either the District level or the Immunization Program level with the provider, before additional vaccine inventory is released. During VFC site visits providers are asked to demonstrate their method of tracking vaccine usage on the Vaccine Accountability Form.
- C. We have instituted an education program for providers to verify that vaccines distributed to providers under the VFC program are administered to VFC eligibles.
- D. We will continue to provide written reports to providers and will also provide written reports to the district offices.
- E. We have made it a requirement that all providers screen children for VFC eligibility. This screening is monitored through VFC site visits by Immunization Program staff. We will require corrective actions when this requirement is not met and will conduct follow-up site visits to ensure that corrective actions are undertaken.
- F. We will document in writing all issues of non-compliance discovered in our reviews of selected patient files.
- G. A change in the reporting process documents all of the issues identified during the site visit.

Finding 2004 – 20, Continued

Management's Response, Continued

- H. Since January 2004 vaccine management protocols are required. If a practice lacks one, a corrective action plan with a timeline for implementation is established.
- I. We acknowledge that the reviewer should have cited the provider for using the vaccines inappropriately and required as a corrective action that the vaccines be replaced, which ultimately was done.
- J. Provider practice sites have been given written and oral instructions as to the elements that must be recorded for each vaccination administered, a new form has been provided to assist in the process, and charts are audited at site visits for conformity to the standards required. The most common element previously missing was the recording of the VIS publication date. We agree that these issues should be reported to the provider in writing.
- K. We have instituted a reconciliation process and agree we should meet the standard.
- L. The reconciliation process in (K) above applies to this finding. We should meet the standard.

Scheduled Completion Date: June 30, 2005.

Contact Person: Patrick Burke, Federal Grants Administrator, Department of Health, (802) 863-7257.

Finding 2004 – 21

Agency of Human Services

Immunization Grants (CFDA #93.268)

Requirement

Effective control and accountability must be maintained for all vaccine. Vaccine must be adequately safeguarded and used solely for authorized purposes.

Condition Found

The Department acts as the centralized depot for all vaccines for enrolled providers, in that those providers are also able to obtain all their required vaccines from the State of Vermont in addition to the Vaccines For Children (VFC) program. All vaccines are initially received directly by the Department of Health. On an as needed basis, vaccines are distributed to the Department's eleven area District Offices based on order requests prepared directly by the District Office. The District Office then releases the funds to enrolled providers based on the number of doses requested on a Vaccine Accountability Sheet. All vaccines are identifiable based upon a lot number assigned to the vaccine by the manufacturer.

During our testwork over the procedures in place to safeguard vaccines, we noted the following:

- A. The Department does not monitor to ensure that its District Offices stores VFC and 317 funded vaccines separately from vaccines funded through State funds. As such, there are no mechanisms in place to ensure that the vaccines received by the Centers for Disease Control (CDC) as part of the Immunization Grant Program were properly distributed as such to the provider.
- B. While it appears based on the questionnaires completed during the Department's on site review that the provider stores State supplied vaccines separately from privately purchased vaccines, the State does not monitor to ensure that the provider stores VFC and 317 funded vaccines separately from other vaccines provided by the State. In addition, the Department does not ensure that the lot number administered by the provider agree to the lot numbers shipped to the provider by the District Office.

Finding 2004 – 21, Continued

C. The Department completes a monthly inventory reconciliation of the vaccine inventory on hand to the balance as stated in the VACMAN system, the inventory tracking system provided by the Centers for Disease Control (CDC). The Department notifies the CDC that the inventory reconciliation has been completed and provides CDC with this inventory on hand information. Up until January 2004, the Department did not maintain any formal documentation to substantiate their inventory claim. In January 2004, they began to keep a hard copy of the VACMAN inventory report. However, there was no supporting documentation for any discrepancies between the VACMAN inventory report and the actual inventory counts, nor did the Department maintain the e-mail notification to CDC regarding the inventory claim for that month. As such, there are no mechanisms in place to allow us to verify that a monthly reconciliation of the inventory was being performed for the first half of the State Fiscal Year 2004 and that any adjustments made to the inventory balance was proper.

The instances noted above appear to be systemic compliance deficiencies. The lack of procedures over the safeguarding of vaccines could result in vaccines being utilized at both the provider and District Office locations for participants not eligible to receive vaccines under the Federal program.

This finding is considered to be a material weakness.

Questioned Costs

Not determinable.

Recommendations

We recommend that the Department implement the necessary policies and procedures to ensure that all federally funded vaccines are properly safeguarded at both the Department, District Office and provider sites.

Management's Response

Steps to Correct:

We believe that we do store separately vaccines purchased with federal funds versus state purchased vaccines. The state purchased vaccines are of a different vaccine type.

Finding 2004 – 21, Continued

Management's Response, Continued

Lot numbers of vaccines administered are recorded on the accountability sheets and tracked in the computer system by provider site and the lot numbers distributed to them. The provider records the lot number administered in the patient's chart and in the Vermont Immunization Registry (in practices where the registry has been implemented.). In January 2004 this process changed to maintain paper copies of the email notification to CDC of the actual inventory counts. We will keep a paper copy of the monthly email submission to CDC of our VACMAN inventory report. We will also keep a paper copy of the document showing the monthly adjustments to the inventory report.

Scheduled Completion Date: June 30, 2005.

Contact Person: Patrick Burke, Federal Grants Administrator, Department of Health, (802) 863-7257.

Finding 2004 – 23

Agency of Human Services

Block Grants for Prevention and Treatment of Substance Abuse (CFDA #93.959)

Requirement

The State must provide for independent peer reviews which assess the quality, appropriateness, and efficacy of treatment services provided to individuals. At least 5 percent of the entities providing services in the State shall be reviewed. The State shall ensure that the peer reviewers are independent by ensuring that the peer review does not involve reviewers reviewing their own programs and the peer review is not conducted as part of the licensing or certification process. (42 USC 300x-53; 45 CFR section 96.136)

Condition Found

During our testwork over the independent peer review process, we noted that there are currently no programs or processes in place to ensure regular independent peer review of treatment provider's facilities in the State of Vermont and there are no systems in place to ensure that five percent of treatment providers are reviewed annually. While some providers receive an accreditation from the Commission for Accreditation of Rehabilitation Facilities (CARF) or from the Joint Commission on Accreditation of Healthcare Organizations (JCAHO) appear to satisfy the above requirement, entities that do not seek CARF or JCAHO accreditation will not be reviewed. We further noted that twenty out of twenty-five treatment provider's facilities that the Department did not obtain a CARF or a JCAHO accreditation.

This appears to be a systemic compliance deficiency. The lack of independent peer reviews could hinder the Department's ability to adequately monitor the treatment services provided by the treatment facility and could lead to unallowable costs charged to the Federal grant.

This finding is considered to be a material weakness.

Questioned Costs

None noted.

Recommendation

We recommend that the Department implement the necessary policies and procedures to ensure that a system of independent peer reviews is implemented to properly monitor the treatment provided to individuals by the treatment providers throughout the State that receives federal funding under this program.

Finding 2004 – 23, Continued

Management's Response

Steps to Correct:

We agree that the Department did not have peer reviews and did not review the required five percent of treatment providers in FY04. For FY05, the peer review requirement no longer applies. The position that has primary responsibility for the Health Department reviews was vacant through FY04. The position was finally filled June 14, 2004, which corrects this deficiency. Since then, all of the treatment providers have been reviewed. Our goal is to review 100% of providers in a year, rather than the 5% required as a minimum. In addition, there are currently nine providers who have accreditation from CARF or JCAHO as well as having been reviewed by the Health Department.

Scheduled Completion Date: June 30, 2006.

Contact Person: Patrick Burke, Federal Grants Administrator, Department of Health, (802) 863-7257.

Finding 2004 – 24

Agency of Human Services

Block Grants for Prevention and Treatment of Substance Abuse (CFDA #93.959)

Requirement

A pass-through entity is responsible for:

- Identifying to the subrecipient the Federal award information (e.g., CFDA title and number, award name, name of Federal agency) and applicable compliance requirements.
- Monitoring the subrecipient's use of Federal awards through reporting, site visits, regular contact, or other means to provide reasonable assurance that the subrecipient administers Federal awards in compliance with laws, regulations, and the provisions of contracts or grant agreements and that performance goals are achieved.
- Ensuring that subrecipient's expending \$300,000 (\$500,000 for fiscal years ending after December 31, 2003 as provided in OMB Circular A-133, as revised) or more in Federal awards during the subrecipient's fiscal year have met the audit requirement of OMB Circular A-133 and that the required audits are completed within nine months of the end of the subrecipient's audit period, issuing a management decision on audit findings within six months after receipt of the subrecipient's audit report, and ensuring that the subrecipient takes timely and appropriate corrective action on all audit findings. In cases of continued inability or unwillingness of a subrecipient to have the required audits, the pass-through entity shall take appropriate action using sanctions.
- Evaluating the impact of subrecipient activities on the pass-through entity's ability to comply with applicable Federal regulations.

Condition Found

Funds granted under the Substance Abuse Prevention and Treatment Block Grant (SAPT) are to be used for planning, carrying out and evaluating activities to prevent and treat substance abuse and other related activities. As the State does not own or operating its own substance abuse treatment facility, it grants funds to external parties to provide specified prevention and treatment services. During our testwork over the monitoring process, we noted the following:

Finding 2004 – 24, Continued

- A. The Notice of Grant Award should contain information regarding the CFDA title and number, the amount of the award as it relates to the CFDA number, the name of the Federal Agency, requirements imposed by laws, regulations, and the provisions of contract or grant agreements. We noted two out of twenty-five grant award documents did not contain the CFDA number or the title of the program and therefore, it could not be determined the amount of the grant which related to the Substance Abuse Prevention and Treatment Block Grant. A coding/cover sheet is then prepared for each invoice and details the amount authorized to be paid under a certain program code, the expenditure code, and the funding source code. For each of these grants the entire amount of the invoice was paid and charged to the federal program code, however it could not be determined how much of that invoice should have actually been charged to the program.
- B. Each subrecipient providing treatment services is required to provide audited financial statements and when applicable, a single audit report. The Department does not have the procedures to determine whether or not the subrecipient is a for profit and non-profit entity that would be subjected to the requirements of OMB Circular A-133. As a result the Department is unable to monitor whether or not a provider should have submitted a single audit report. During our testwork, we noted eight out of the twenty-five subrecipients had submitted financial statements, ten out of twenty-five had submitted OMB Circular A-133 audits, one out of twenty-five had submitted a financial proposal and five out of twenty-five did not submit any audits as these awards related to preventing substance abuse and the Department does not require these providers to submit annual reports.
- C. The Notice of Grant Award contains information regarding the source of funding that details how much of the grant award relates to the CFDA 93.959. A coding/cover sheet is then prepared for each invoice and details the amount authorized to be paid under a certain program code, the expenditure code, and the funding source code. Per review of seven out of the twenty-five coding/cover sheets and invoices, we noted that the entire amount of the invoice was charged to the federal code for the program. Per review of the grant award document for these seven invoices, it appeared that the State had over expended the authorized amount as it relates to CFDA 93.959.
- D. Monthly utilization reports are submitted to the Department via electronic tapes. The Department receives the monthly information and compiles it into an annual summary report which is filed with the SYNAR report. However, there is no evidence maintained of these monthly utilization reports by the Department.
- E. Each subrecipient is required to sign statements of assurances as provided per the grant agreement. These assurances contain various standards that the Department requires them to follow over expending the Block grant monies. In addition, it contains a clause over the suspension and debarment. We noted that for four of the twenty-five subrecipients there was not a signed statement of assurance that contained the clause over the suspension and debarment.

Finding 2004 – 24, Continued

The above instances noted appear to be systemic compliance deficiencies. The lack of procedures in place to monitor providers increases the risk that the Department would not be able to identify control deficiencies for their providers which could lead to unallowable costs being charged to the grant.

This finding is considered to be a material weakness.

Questioned Costs

\$42,559

Recommendation

We recommend that the Department implement the necessary policies and procedures to monitor subrecipients to help ensure accurate compliance with federal regulations.

Management's Response

Steps to Correct:

- A. The two grant award documents cited did not contain the required A-133 advice to the subgrantee about federal funds. This appears to have been simply due to clerical error. The Department has a procedure for review of the grant award documents before they are signed, and as a corrective action staff will be attentive during this review to the possibility of missing information on the award. We do not dispute the need to display this information; however it is worth noting that the information that would normally have been present is not intended to be a control mechanism. It is intended to be advisory information to the subrecipient, providing the Department's best estimate of the amount of federal reimbursement that will ultimately fund this grant award.

- B. The Department does try to determine whether or not a subgrantee is a non-profit entity. Our general practice is to make grants only to non-profit entities, so the existence of a grant award should indicate that the Department believes that the entity in question is a non-profit. In the case of SAPT payments, we also need to know the non-profit status because federal SAPT funds cannot be used for for-profit entities. Although all of the entities receiving SAPT funds through a grant mechanism can be assumed to be non-profit, the Health Department does not know whether the expenditure threshold has been met by the entity or whether the Health Department is the cognizant agency for the entity. Procedures have been implemented in FY05 by the Finance Dept. to address these issues.

Finding 2004 – 24, Continued

Management's Response, Continued

- C. The finding is correct in stating that the grant award contains information regarding our expected ultimate amounts of state and federal funding that will support the award. As noted in (A) above, this advisory information is not intended to be a control mechanism. Rather, it is our best information as to the amount of federal funding that might be applied to the award through the course of the award period. The actual distribution of expenditures to state and federal fund sources depends on the grand total of all Department SAPT expenditures that will occur during the year and on the final federal grant award, which may be larger or smaller than initially anticipated. These amounts are not known until well after the grant award is issued. As payments are made, the total costs are charged to the federal grant because all of the costs are eligible, and for this reason, we do not agree that any of these costs should be questioned. These costs are charged to SAPT even though we will not know what share of these total costs will ultimately be supported by federal funds. We note that A-133 states that, "when some of this information is not available, the pass-through entity shall provide the best information available to describe the Federal award." (§ __.400[d][1]) This language seems consistent with our current practice of giving our best estimate at the time the grant award is issued and then charging all eligible costs to the federal grant even though there is no expectation that the federal grant will ultimately cover all costs.
- D. Utilization reports are submitted to the Department monthly. They are submitted electronically, via email. These particular data are not related to SYNAR reports. The Department takes the emailed data and merges them into our database. We will establish a practice of saving the emailed file separately for one year.
- E. We agree that the previous statement of assurance did not require a signature assuring compliance with suspension and debarment regulations. The form has since been changed and these compliance items are now included in the signed statement of assurance.

Scheduled Completion Date: June 30, 2006.

Contact Person: Patrick Burke, Federal Grants Administrator, Department of Health, (802) 863-7257.