



STATE OF ILLINOIS
OFFICE OF THE
AUDITOR GENERAL

William G. Holland, Auditor General

SUMMARY REPORT DIGEST

DEPARTMENT OF HUMAN SERVICES

Financial Audit For the Year Ending June 30, 2012

Summary of Findings:

Total this report 7

Total last report 5

Release Date: May 15, 2013

Repeated from last report: 5

SYNOPSIS

- Weaknesses were identified in the Departments preparation of the generally accepted accounting principle (GAAP) reporting forms submitted to the Illinois Office of the Comptroller and preparation of year-end financial statements.
- The Department did not maintain adequate controls over the calculation and payment of its 2011 prompt payment interest expenditures and failed to timely recover overpayments paid to vendors during the current audit period.
- The Department did not timely file the necessary financial information for fiscal year 2012 with the Illinois Office of the Comptroller.
- The Department's accounts receivable reporting system is cumbersome, relies on numerous subsystems, and requires manual entries.

{Expenditure and Activity Measures are summarized on the reverse page.}

DEPARTMENT OF HUMAN SERVICES
FINANCIAL AUDIT
For The Year Ended June 30, 2012

FINANCIAL INFORMATION - Governmental funds (in thousands)	FY 2012	FY 2011
REVENUES		
Program revenue: charges for service.....	\$ 58,380	\$ 57,248
Program revenue: operating grants.....	4,811,744	4,850,954
General revenue: taxes, interest and other.....	7,847	6,003
Total revenue (1).....	<u>\$ 4,877,971</u>	<u>\$ 4,914,205</u>
EXPENDITURES		
Health and social services.....	\$ 8,282,078	\$ 8,289,396
Debt service - principle.....	360	439
Debt service - interest.....	86	59
Capital outlays	10,479	14,123
Total expenditures (2).....	<u>\$ 8,293,003</u>	<u>\$ 8,304,017</u>
OTHER SOURCES (USES)		
Appropriations from State resources.....	\$ 3,541,699	\$ 3,982,194
Transfers in.....	112,602	87,590
Transfers out.....	(83,061)	(72,343)
Receipts collected & transmitted to the State treasury.....	(90,241)	(609,948)
Lapsed appropriation.....	(60,059)	(46,576)
Other.....	(60,133)	(72,254)
Total other sources (uses) (3).....	<u>\$ 3,360,807</u>	<u>\$ 3,268,663</u>
FUND BALANCE		
Increase (decrease) in fund balance (1) - (2) + (3).....	\$ (54,225)	\$ (121,149)
Fund balance July 1.....	17,822	138,170
Increase (decrease) for changes in inventories.....	(1,539)	801
Fund balance June 30.....	<u>\$ (37,942)</u>	<u>\$ 17,822</u>
SELECTED ACCOUNT BALANCES - June 30, Governmental funds (in thousands)		
	FY 2012	FY 2011
ASSETS		
Cash and cash equivalents & investments.....	\$ 252,739	\$ 186,094
Due from other governments - federal & local.....	240,790	237,179
Loans, taxes and other receivables, net.....	57,126	53,395
Due from other Department and State funds.....	92,685	74,644
Inventories.....	8,682	10,221
Unexpended appropriations.....	417,835	458,954
Total assets.....	<u>\$ 1,069,857</u>	<u>\$ 1,020,487</u>
LIABILITIES		
Accounts payable and other liabilities.....	\$ 754,253	\$ 662,738
Unearned revenue.....	103,343	94,206
Due to other funds - State, federal, local & Department.....	126,526	97,724
Unavailable revenue.....	123,677	147,997
Total liabilities.....	<u>\$ 1,107,799</u>	<u>\$ 1,002,665</u>
FUND BALANCE (DEFICIT)		
Fund balance (Deficit).....	\$ (37,942)	\$ 17,822
Total liabilities and fund balance.....	<u>\$ 1,069,857</u>	<u>\$ 1,020,487</u>
SECRETARY		
During the Audit Period and Currently: Michelle R. B. Saddler		

INTRODUCTION

This report presents our Department-wide financial statement audit for the year ended June 30, 2012. At June 30, 2012 the Department operated 7 Developmental Centers, 8 Mental Health Centers, 2 combined Mental Health and Developmental Centers and 3 Rehabilitation Services Facilities. During the engagement period the Department closed Tinley Park Mental Health Center. The findings are presented in the report beginning at page 51.

FINDINGS, CONCLUSIONS, AND RECOMMENDATIONS

WEAKNESSES IN PREPARATION OF GAAP REPORTING FORMS AND FINANCIAL STATEMENTS

The Department of Human Services' (Department's) year-end financial reporting in accordance with generally accepted accounting principles (GAAP) to the Illinois Office of the Comptroller contained numerous inaccuracies and errors which resulted in changes being made to originally submitted information. Some of the conditions identified follow:

Financial reporting forms contained numerous errors and complete draft of Department financial statements was late

- GAAP reporting packages contained numerous inaccuracies and required corrections which delayed audit testing of the financial statements and the Schedule of Federal Awards prepared by the Department. Auditors did not receive a complete draft of the financial statements and footnotes from the Department until November 26, 2012, approximately one month late.

Current year receivables and deferred revenue from the federal government were overstated by \$45.443 million

- The auditors noted the Department had not properly accounted for amounts due from the federal government and deferred revenue in the DHS Special Purposes Trust Fund (Fund 0408) and the General Revenue Fund (Fund 0001). Federal revenue was deposited in the amount of \$45.443 million into the DHS Special Purposes Trust Fund (Fund 0408) for expenditures that were incurred in the General Revenue Fund (Fund 0001). The Department recorded the amount as due from other funds in Fund 0001. However, an amount due from the federal government was also recorded for the same amount which is not correct as the monies had already been received from the federal government and deposited into Fund 0408. This resulted in an overstatement of the receivable from the federal government and deferred revenue in the amount of \$45.443 million. The Grant/Contract Analysis Form and the financial statements were revised as a result.

An estimated \$3.262 million in lapse period draws should not have been included in the calculation of deferred revenue – unavailable

- The auditors noted the Department included an estimated \$3.262 million in lapse period draws when preparing the Grant/Contract Analysis Form for purposes of calculating

deferred revenue – unavailable in the Community Mental Health Medicaid Trust Fund (Fund 0718). This amount was not drawn in lapse period and should not have been included. The Department of Healthcare and Family Services initiates the draws of federal revenue into this fund and provides the Department with the amounts drawn. The spreadsheet provided to the Department was misinterpreted by Department personnel when preparing the reporting package. As a result, deferred revenue was understated by \$3.262 million and federal operating grants were overstated by \$3.262 million in the Governmental Fund Statements.

- The Department paid fiscal year 2011 prompt payment interest at the erroneous rate of 2% rather than at 1% to 983 vendors. The funds overpaid totaled \$5.380 million. This error was discovered by the Department in January 2012; however, the receivable to recoup these funds was not recorded in the original GAAP reporting package for Fund 0001. Consequently, the Department underpaid a significant portion of fiscal year 2011 prompt payment interest to other vendors as a result of the overpayments. Therefore, in conjunction with the additional adjustment for the receivables, the Illinois Office of the Comptroller posted an adjustment to Fund 0001's GAAP reporting package to record the additional payables of \$7.608 million to 727 vendors. See finding 12-2 for additional detail.

Payroll expenditures were not timely posted to the accounting system for nineteen fund reporting packages totaling \$196.816 million

- The Department had not timely posted payroll expenditure amounts to their accounting system. The reports which support financial reporting data had to be adjusted to include expenditures for the May and June 2012 payroll periods that were not posted. This occurred in nineteen fund reporting packages for a total of \$196.816 million in payroll expenditures. (Finding 12-1, pages 51-54)
This finding was first reported in 2009.

We recommended the Department implement procedures and cross-training measures to ensure GAAP Reporting Packages are prepared in a timely, accurate and complete manner.

Department agrees with auditors

Department officials agreed with the recommendation. (For the previous Department response, see Digest Footnote #1.)

INADEQUATE CONTROLS OVER PROMPT PAYMENT INTEREST

The Department did not maintain adequate controls over the calculation and payment of its 2011 prompt payment interest (PPI) expenditures. In addition, the Department failed to timely recover overpayments paid to vendors during the current audit period.

Receivables and liabilities for 2011 prompt payment expenditures (totaling \$5.830 and \$7.608 million, respectively) were not recorded in the General Revenue Fund's original GAAP reporting package

The auditors requested supporting documentation to verify the Department's accrual of the accounts receivable balance and accounts payable balance reported in the General Revenue Fund 2012 GAAP reporting package. The supporting documentation provided to the auditors indicated the Department had not recorded an accounts receivable adjustment for the General Revenue Fund relating to an erroneous overpayment of PPI paid out to 983 vendors, totaling \$5.380 million, during December 2011. In addition, the auditors noted the Department had not recorded an accounts payable adjustment for the General Revenue Fund relating to 727 vendors, totaling \$7.608 million, not being paid PPI due to the overpayment of PPI and a lack of appropriation authority. On November 7, 2012, the Department instructed the Office of the Comptroller to post an adjustment to the General Revenue Fund GAAP reporting package to record both the additional receivable of \$5.380 million and the additional payable of \$7.608 million.

Additional audit procedures

The auditors conducted additional auditing procedures in order to assess what had caused the overpayments to be paid out and what the Department's procedures were for recouping the \$5.380 million from the 983 vendors and to ensure the Department's established policies and procedures were followed.

Laws and regulation governing PPI

During fiscal year 2011, the Department had two applicable interest penalty rates. Certain medical assistance payments (bills submitted under Article V of the Illinois Public Aid Code (305 ILCS 5/5-1 et seq.)) were required to be paid at an interest penalty rate of 2% per month. All other bills were to be paid at an interest penalty rate of 1% per month. P.A. 97-72, effective for fiscal year 2012, eliminated the variance in rates thereby returning all interest penalties to the rate of 1%.

Overpayments to 983 vendors were a result of a formula error within the newly developed PPI calculation program

The auditors discovered the overpayments to the 983 vendors were a result of a formula error within the newly developed PPI calculation program at the Department. As the PPI laws and regulations had changed from the previous years, the Department was unable to calculate the 2011 PPI due to vendors at fiscal year-end in the same system which it previously had for 2010. Development of the new PPI program was completed in December 2011 (FY12). Within the new program utilized for 2011 PPI, an inaccurate formula was used which resulted in the enhanced medical assistance rate of 2% being applied to 983 ineligible vendors.

Overpayments discovered by the Department in January 2012

Department personnel discovered the error of overpaying PPI during January 2012 at which time they promptly brought the matter of the overpayments to the attention of management. Management developed a corrective action plan dated January 26, 2012 and shared it with staff on January 30, 2012.

Department developed a corrective action plan in January 2012

Department began collection activity in March 2013 which was 14 months after the overpayments were discovered

The corrective action plan included a collection step to contact the vendors receiving the largest overpayments immediately by telephone to advise that the payments should be returned. The Department calculated 60 vendors which accounted for approximately 84% of the total overpayments. The corrective action plan was discussed at regular meetings held during the months of February 2012 through July 2012. However, no action was taken to establish the accounts receivable within the Department's Consolidated Accounting and Reporting System and begin collection activity until after March 6, 2013, over 14 months from the time the overpayments were discovered, even though staff repeatedly asked for guidance and approval from management to begin.

(Finding 12-2, pages 55-58)

We recommend Department management provide timely guidance to its staff and thoroughly review new or revised application programs before implementation. Further, the Department should follow established policies and procedures for recording overpayments as receivables and billing to ensure the likelihood that all State funds are eventually recouped.

Department Response

Department officials partially agreed with the recommendation and stated this error was the result of lack of staffing. The decision to postpone the collection of this overpayment was made due to the fact that the same providers that received an overpayment collectively were owed \$522 million. Management did not ignore staff in correcting the overpayment issue it was a conscious decision that due to lack of staff and the GAAP packages and financials deadline at the same time we chose to postpone the collection of the overpayments. If the back payments to providers were up to date, a different decision to pursue collection activities immediately would have been made. Currently, providers are owed over \$500 million and under these circumstances we do not believe collectability will be an issue. We are currently working with the legislature on writing legislation that will allow DHS to offset 2012 prompt payment interest with the overpayment.

Auditor's Comment

In an Auditor's Comment, we noted the FY12 GAAP reporting package preparation process would normally begin during the first few weeks of July 2012, which is several months after the January 2012 date when the Department discovered the overpayment problem. The auditors obtained information from various Department staff members regarding the overpayments and the need to establish an accounts receivable. In fact, staff members within the Bureau of Collections set up a receivable code in the Department's Consolidated Accounting and Reporting System in late January 2012.

The Department has established policies and procedures to recover overpayments which are standardized and ensures proper internal controls are in place to recoup funds due to the State in a timely manner. In this instance, management did not follow those procedures and delayed the collection of \$5.380 million for over a year. In addition, not all vendors who were overpaid were service providers. The list of vendors who were overpaid FY11 PPI also included vendors who had performed other operational and administrative services for the Department.

The Illinois Office of Comptroller issues guidance on establishing, reporting and collecting amounts owed to the State in the Statewide Accounting Management System Manual (SAMS Manual Procedures 26.10.10 through 26.40.80). SAMS Manual Procedure 26.20.10 requires an accounts receivable to be created when goods are delivered, services are performed or when the State's claim for future cash is reasonably estimable. Taking 14 months to initiate collection procedures clearly is an inordinate amount of time and deviates from State requirements.

Department did not timely file necessary financial information with the Comptroller

NONCOMPLIANCE WITH STATUTORY REQUIREMENTS FOR FISCAL REPORTING

The Department did not timely file the necessary financial information for fiscal year 2012 with the Illinois Office of the Comptroller (Comptroller).

Department submitted complete financial statements to the auditor on November 26, 2012, approximately one month late from the statutory deadline of October 31, 2012

The State Comptroller Act (Act) (15 ILCS 405/19.5) requires State agencies to report, on or before October 31, 2012, all financial information as directed by the Comptroller in order to compile and publish a comprehensive annual financial report (CAFR) in accordance with generally accepted accounting principles (GAAP).

The auditors noted several weaknesses in the preparation of GAAP reporting forms and year-end Department financial statements. See finding and recommendation 12-1 beginning on page 51. Among the weaknesses noted was the late submission of the Department's financial statements to the auditors on November 26, 2012. Likewise, in a letter dated November 5, 2012, the Comptroller notified the Department about items that had not been received as of October 31, 2012. These items included: 1) draft financial statements as of June 30, 2012, 2) responses to review comments relating to the GAAP package submission for the General Revenue Fund, and 3) revisions to the form SCO-538 for reporting information on capital assets.

The Department submitted a report and action plan on November 15, 2012

In response to the letter, the Department submitted a report and action plan on November 15, 2012 to the Comptroller, the Auditor General, the Office of the Governor, the Speaker and Minority Leader of the House of Representatives, and the President and Minority Leader of the Senate. (Finding 12-3, pages 59-60)

We recommend the Department implement procedures and cross-training measures to ensure required financial information is prepared in a timely, accurate and complete manner. This should include allocating sufficient staff resources and the implementation of formal procedures to ensure financial information is prepared and submitted to the Comptroller in a timely and accurate manner, and that all supporting documentation is maintained in a contemporaneous manner.

Department agrees with auditors

Department officials agreed with the recommendation and noted they will implement procedures and cross-training measures to ensure GAAP Reporting Packages are prepared in a timely, accurately and complete manner.

WEAKNESSES OVER QUARTERLY REPORTING OF ACCOUNTS RECEIVABLE

Compiling accounts receivable information is complex and cumbersome

During testing of the quarterly receivable forms, the auditors noted the reports were manually compiled from multiple accounts receivable systems in order to issue a single report. The compilation is complex and cumbersome and, as a result, there is a potential for errors in reporting.

Unreconciled differences

Auditors noted the quarterly accounts receivable reports submitted to the Comptroller contained differences that could not be reconciled with the Department's supporting documentation. Auditors reviewed the supporting documentation for these receivables but were unable to reconcile the amounts to the totals reported for the quarter end. For fiscal year 2012, differences ranged from \$20 million to \$37 million at the end of each quarter.

Limitations in the current systems

The Department has developed formal written policies and procedures to document its existing system and cross-trained other workers on preparing the required reports. It appears there is a methodology for accumulating quarterly accounts receivable information, but limitations in current systems make it cumbersome and difficult to support. (Finding 12-4, pages 61-62) **This finding was first reported in 2007.**

We recommended the Department implement a Department-wide accounts receivable system, working with the appropriate parties regarding any possible state-wide consolidated accounting system initiatives.

Department agrees with auditors

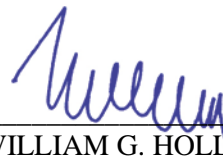
Department officials agreed with the recommendation and continue to review the accounts receivable agency wide. (For the previous Department response, see Digest Footnote #2.)

OTHER FINDINGS

The remaining findings pertain to: (1) inadequate controls over commodities, (2) outdated and insufficient commodity inventory system, and (3) inadequate controls over capital asset financial reporting. We will review the Department's progress towards the implementation of our recommendations in our next engagement.

AUDITORS' OPINION

The auditors stated the Department's financial statements as of June 30, 2012 and for the year then ended were presented fairly in all material respects.



WILLIAM G. HOLLAND
Auditor General

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SPECIAL ASSISTANT AUDITORS

Sikich LLP were our Special Assistant Auditors for this engagement.

DIGEST FOOTNOTES

#1 - WEAKNESSES IN PREPARATION OF GAAP REPORTING FORMS AND FINANCIAL STATEMENTS – Previous Department Response

2011: The Department agrees with the recommendation. DHS will implement procedures to cross-train employees to help ensure GAAP packages are prepared timely and accurately. Additionally, DHS is in the process of hiring staff to be utilized in the GAAP reporting process.

2 - WEAKNESSES OVER QUARTERLY REPORTING OF ACCOUNTS RECEIVABLE – Previous Department Response

2011: The Department accepts the recommendation. The Department is reviewing the Accounts receivable agency wide. Based on the results of the review, the Department indicated they will establish and implement any changes as solutions occur.