

# California State Auditor

B U R E A U O F S T A T E A U D I T S

## **State of California:**

*Internal Control and State and Federal  
Compliance Audit Report for the  
Fiscal Year Ended June 30, 2001*



March 2002  
2001-002

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# CALIFORNIA STATE AUDITOR

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ELAINE M. HOWLE  
STATE AUDITOR

STEVEN M. HENDRICKSON  
CHIEF DEPUTY STATE AUDITOR

March 22, 2002

2001-002

The Governor of California  
President pro Tempore of the Senate  
Speaker of the Assembly  
State Capitol  
Sacramento, California 95814

Dear Governor and Legislative Leaders:

As required by the California Government Code, Section 8542 et seq., the Bureau of State Audits presents its audit report concerning our review of the State of California's internal controls and compliance with state and federal laws and regulations for the year ended June 30, 2001.

This report concludes that the State continues to experience certain problems in accounting and administrative practices that affect its internal controls over financial reporting and over compliance with federal requirements. As a result, the State has not always complied with some state and federal regulations. Although none of the problems we identified is significant to the State's financial statements or the federal programs it administers, weaknesses in the State's internal control system could adversely affect its ability to provide accurate financial information and to administer federal programs in compliance with applicable requirements.

Respectfully submitted,

ELAINE M. HOWLE  
State Auditor

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# **AUDITOR'S SECTION**

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## **Independent Auditor's Reports on Compliance and Internal Control**

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# CALIFORNIA STATE AUDITOR

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ELAINE M. HOWLE  
STATE AUDITOR

STEVEN M. HENDRICKSON  
CHIEF DEPUTY STATE AUDITOR

## **Independent Auditor's Report on Compliance and on Internal Control Over Financial Reporting Based on an Audit of Financial Statements Performed in Accordance With Government Auditing Standards**

The Governor and the Legislature of  
the State of California

We have audited the general purpose financial statements of the State of California as of and for the year ended June 30, 2001, and have issued our report thereon dated November 16, 2001. We did not audit the financial statements of certain capital projects funds, which reflect total assets and revenues, constituting 59 percent and 66 percent, respectively, of the capital projects funds. In addition, we did not audit the financial statements of certain enterprise funds, including those of the California State University, which reflect total assets and revenues, constituting 94 percent and 95 percent, respectively, of the enterprise funds. We did not audit the financial statements of certain internal service funds, which reflect total assets and revenues, constituting 22 percent and 44 percent, respectively, of the internal service funds. We also did not audit the financial statements of the pension trust funds, which reflect total assets constituting 85 percent of the fiduciary funds. Finally, we did not audit the University of California funds or the financial statements of certain component unit authorities, which reflect total assets and revenues, constituting 95 percent and 93 percent, respectively, of the component unit authorities. The financial statements of certain capital projects, enterprise and internal service funds, the pension trust funds, the University of California funds, and certain component unit authorities referred to above were audited by other auditors whose reports have been furnished to us, and our opinion, insofar as it relates to the amounts included for these funds and entities, is based solely upon the reports of the other auditors. We conducted our 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 of America.

### **COMPLIANCE**

As part of obtaining reasonable assurance about whether the State of California's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grants, 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 our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance that are required to be reported under *Government Auditing Standards*.

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#### BUREAU OF STATE AUDITS

## INTERNAL CONTROL OVER FINANCIAL REPORTING

In planning and performing our audit, we considered the State of California's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on the internal control over financial reporting. However, we noted certain matters involving the internal control over financial reporting and its operation that we consider to be reportable conditions. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over financial reporting that, in our judgment, could adversely affect the State of California's ability to record, process, summarize, and report financial data consistent with the assertions of management in the financial statements. Reportable conditions are described in the accompanying schedule of findings and questioned costs as items 2000-19-1 through 2000-19-11.

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 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 consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses. However, we believe none of the reportable conditions described above is a material weakness.

This report is intended solely for the information and use of the governor and Legislature of the State of California, the management of the executive branch, and the federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

BUREAU OF STATE AUDITS



PHILIP J. JELICICH, CPA  
Deputy State Auditor

November 16, 2001



# CALIFORNIA STATE AUDITOR

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ELAINE M. HOWLE  
STATE AUDITOR

STEVEN M. HENDRICKSON  
CHIEF DEPUTY STATE AUDITOR

## **Independent Auditor's Report on Compliance With Requirements Applicable to Each Major Program and on Internal Control Over Compliance in Accordance With OMB Circular A-133**

The Governor and the Legislature of  
the State of California

### **COMPLIANCE**

We have audited the compliance of the State of California with the types of compliance requirements described in the *U. S. Office of Management and Budget (OMB) Circular A-133 Compliance Supplement* that are applicable to each of its major federal programs for the year ended June 30, 2001. The State of California's major federal programs are identified in the summary of the auditor's results section of the accompanying schedule of findings and questioned costs. Compliance with the requirements of laws, regulations, contracts, and grants applicable to each of its major federal programs is the responsibility of the State of California's management. Our responsibility is to express an opinion on the State of California's compliance based on our audit.

The State of California's general purpose financial statements include the operations of the University of California and the California State University systems, as well as the California Housing Finance Agency, a component unit authority of the State. However, these entities are not included in the accompanying schedule of findings and questioned costs or schedule of federal assistance for the year ended June 30, 2001. The University of California and the California State University systems, and the California Housing Finance Agency, which reported expenditures of federal awards totaling \$2.1 billion and \$971.3 million, and \$68.9 million, respectively, engaged other auditors to perform an audit in accordance with OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations* (OMB Circular A-133).

We conducted our audit of compliance in accordance with generally accepted auditing standards; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and OMB Circular A-133. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about the State of California's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We

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### BUREAU OF STATE AUDITS

believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination of the State of California's compliance with those requirements.

In our opinion, the State of California complied, in all material respects, with the requirements referred to above that are applicable to each of its major federal programs for the year ended June 30, 2001. However, the results of our auditing procedures disclosed instances of noncompliance with those requirements, which are required to be reported in accordance with OMB Circular A-133 and which are described in the accompanying schedule of findings and questioned costs. See the attachment for a list of these issues.

### **INTERNAL CONTROL OVER COMPLIANCE**

The management of the State of California is responsible for establishing and maintaining effective internal control over compliance with requirements of laws, regulations, contracts, and grants applicable to federal programs. In planning and performing our audit, we considered the State of California's internal control over compliance with requirements that could have a direct and material effect on a major federal program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance and to test and report on the internal control over compliance in accordance with OMB Circular A-133.

We noted certain matters involving the internal control over compliance and its operation that we consider to be reportable conditions. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over compliance that, in our judgment, could adversely affect the State of California's ability to administer a major federal program in accordance with the applicable requirements of laws, regulations, contracts, and grants. Reportable conditions are described in the accompanying schedule of findings and questioned costs. The attachment also contains a list of these issues.

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 noncompliance with the applicable requirements of laws, regulations, contracts, and grants that would be material in relation to a major federal program being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of the internal control over compliance would not necessarily disclose all matters in the internal control that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses. However, we believe none of the reportable conditions listed in the attachment is a material weakness.

### **SCHEDULE OF FEDERAL ASSISTANCE**

We have audited the general purpose financial statements of the State of California as of and for the year ended June 30, 2001, and have issued our report thereon dated November 16, 2001. We did not audit the financial statements of certain capital projects funds, which reflect total assets and revenues, constituting 59 percent and 66 percent,

respectively, of the capital projects funds. In addition, we did not audit the financial statements of certain enterprise funds, including those of the California State University, which reflect total assets and revenues, constituting 94 percent and 95 percent, respectively, of the enterprise funds. We did not audit the financial statements of certain internal service funds, which reflect total assets and revenues, constituting 22 percent and 44 percent, respectively, of the internal service funds. We also did not audit the financial statements of the pension trust funds, which reflect total assets constituting 85 percent of fiduciary funds. Finally, we did not audit the University of California funds or the financial statements of certain component unit authorities, which reflect total assets and revenues, constituting 95 percent and 93 percent, respectively, of the component unit authorities. The financial statements of certain capital projects, enterprise and internal service funds, the pension trust funds, the University of California funds, and certain component unit authorities referred to above were audited by other auditors whose reports have been furnished to us, and our opinion, insofar as it relates to the amounts included for these funds and entities, is based solely upon the reports of the other auditors.

Our audit was performed for the purpose of forming an opinion on the general purpose financial statements taken as a whole. The accompanying schedule of federal assistance is presented for purposes of additional analysis as required by OMB Circular A-133 and is not a required part of the general purpose financial statements. OMB Circular A-133 requires the schedule of federal assistance to present total expenditures for each federal assistance program. However, although the State's automated accounting system separately identifies receipts for each federal assistance program, it does not separately identify expenditures for each program. As a result, the State presents the schedule of federal assistance on a cash receipts basis. In addition, the schedule of federal assistance does not include expenditures of federal awards received by the University of California and the California State University systems, or the California Housing Finance Agency. These expenditures are audited by other independent auditors in accordance with OMB Circular A-133. The information in the accompanying schedule has been subjected to the auditing procedures applied in the audit of the general purpose financial statements and, in our opinion, is fairly stated, in all material respects, in relation to the general purpose financial statements taken as a whole.

This report is intended solely for the information and use of the governor and Legislature of the State of California, the management of the executive branch, and the federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

BUREAU OF STATE AUDITS



PHILIP J. JELICICH, CPA  
Deputy State Auditor

November 16, 2001

Attachment

## ATTACHMENT

The compliance issues are:

2001-1-1	2001-9-2
2001-2-2	2001-9-6
2001-2-3	2001-12-1
2001-3-1	2001-12-2
2001-3-2	2001-12-6
2001-3-4	2001-12-7
2001-3-5	2001-13-1
2001-3-6	2001-13-2
2001-3-8	2001-13-3
2001-3-9	2001-14-1
2001-5-1	2001-14-2
2001-5-2	2001-14-3
2001-7-2	2001-14-4
2001-8-2	2001-14-5
2001-9-1	2001-14-6

The internal control over compliance issues are:

2001-2-1	2001-9-4
2001-3-3	2001-9-5
2001-3-7	2001-9-6
2001-3-8	2001-9-7
2001-7-1	2001-12-3
2001-8-1	2001-12-4
2001-8-2	2001-12-5
2001-9-2	2001-13-1
2001-9-3	2001-13-3

## **Schedule of Findings and Questioned Costs**

**STATE OF CALIFORNIA  
SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
FOR THE FISCAL YEAR ENDED JUNE 30, 2001**

**Summary of Auditor's Results**

**Financial Statements**

Type of report issued by auditors	Unqualified
Internal control over financial reporting:	
Material weaknesses identified?	No
Reportable conditions identified that are not considered to be material weaknesses?	Yes
Noncompliance material to financial statements noted?	No

**Federal Awards**

Internal control over major programs:	
Material weaknesses identified?	No
Reportable conditions identified that are not considered to be material weaknesses?	Yes
Type of report the auditor issued on compliance for major programs	Unqualified
Any audit findings disclosed that are required to be reported in accordance with Section .510(a) of Circular A-133?	Yes
Dollar threshold used to distinguish between Type A and Type B programs	\$58.6 million
Auditee qualified as low-risk auditee?	No



*Identification of major programs:*

<b>CFDA Number</b>	<b>Name of Federal Program or Cluster of Programs</b>
	Food Stamp Cluster
	Child Nutrition Cluster
	Employment Services Cluster
	JTPA Cluster
	Highway Planning and Construction Cluster
	Student Financial Aid Cluster
	Special Education Cluster
	Aging Cluster
	Child Care Cluster
	Medicaid Cluster
10.550	Food Distribution
10.557	Special Supplemental Nutrition Program for Women, Infants, and Children
10.558	Child and Adult Care Food Program
14.239	HOME Investment Partnerships Program
17.225	Unemployment Insurance
17.253	Welfare-to-Work Grants to States and Localities
17.255	Workforce Investment Act
66.468	Capitalization Grants for Drinking Water State Revolving Fund
83.544	Public Assistance Grants
83.548	Hazard Mitigation Grant
84.010	Title I Grants to Local Educational Agencies
84.011	Migrant Education—Basic State Grant Program
84.048	Vocational Education—Basic Grants to States
84.126	Rehabilitation Services—Vocational Rehabilitation Grants to States
84.181	Special Education—Grants for Infants and Families with Disabilities
84.278	School to Career—Implementation Grants
84.340	Class Size Reduction
93.268	Immunization Grants
93.558	Temporary Assistance for Needy Families
93.563	Child Support Enforcement
93.568	Low-Income Home Energy Assistance
93.658	Foster Care—Title IV-E
93.659	Adoption Assistance
93.667	Social Services Block Grant
93.767	State Children’s Insurance Program
93.917	HIV Care Formula Grants
93.959	Block Grant for Prevention and Treatment of Substance Abuse
93.994	Maternal and Child Health Services Block Grant to the States

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**Compliance and Internal Control Issues  
Applicable to the Financial Statements  
and State Requirements**

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## DEPARTMENT OF HEALTH SERVICES

Reference Number:

2001-19-1

### CONDITION

The Department of Health Services (department) needs to strengthen its controls over the processing of loan payments. It also needs to strengthen controls on the preparation of its revolving fund financial statements. Specifically, the following concerns surfaced during our audit:

- The department did not always maintain accurate records for loan disbursements to local governments. For example, our review of loan contract files noted several instances in which the department did not record loan disbursements in the contract logs. We also noted that the department twice failed to record loan disbursements totaling \$883,000 in its federal reimbursement worksheet. At the time of these disbursements, the worksheet showed the department was eligible to request an additional \$73,000 in federal reimbursement; however, the amount should have been \$956,000.
- The department improperly reported a liability totaling \$539,000 twice in its financial statements. As a result, the amount of liabilities and expenditures reported to the State Controller's Office (SCO) was overstated by \$539,000.
- The department overpaid one loan recipient \$191,000. The overpayment occurred because the department erroneously paid the remaining contract funds still available even though the loan recipient had not submitted invoices for the additional amounts. The loan recipient returned the warrant shortly after it was issued. The department subsequently issued a revolving fund check for the appropriate amount.
- The department understated its interest receivable balance by \$25,000 because it did not properly accrue interest for all loan disbursements. The department bills loan recipients semiannually for interest charges for the six-month periods ending December 31 and June 30. However, because the department prepared the June billings in May and did not accrue interest for five loan disbursements made subsequent to the billing date, interest owed on these five loans was not recorded in its financial statements.
- The department does not properly account for loans made from the revolving fund. In fiscal year 2000-01, the department disbursed loans totaling over \$55 million. However, rather than record the disbursements as loans receivable or loans to other governments, the department expensed all payments to recipients. The department properly accounted for loan principal repayments by reducing the loans receivable balance. But because it had not previously established the loan balance, the department's financial statements reflected a negative balance in the loans receivable account.

## **CRITERIA**

Our review of the Safe Drinking Water State Revolving Fund (revolving fund) determined that the following compliance requirements relate to the department:

The California Government Code, sections 13401 and 13403, requires state agencies to effectively maintain internal accounting and administrative controls. Such controls include accurate record-keeping procedures.

Additionally, the Department of Finance's CALSTARS Procedure Manual, Volume 3, provides uniform procedures for departments that disburse loans to other governmental agencies. Specifically, departments are required to record the disbursements in the State's Loan Principal Disbursement and Loans Receivable accounts on a budgetary basis.

## **RECOMMENDATIONS**

The department should ensure that it records all transactions in its subsidiary records and reviews its financial statements for accuracy. Further, the department should account for loan transactions in accordance with the Department of Finance's CALSTARS Procedure Manual.

## **DEPARTMENT'S VIEW AND CORRECTIVE ACTION PLAN**

The department agrees with our finding and plans to take corrective action. The department stated that it will maintain a separate log for all loan disbursements and will cross-check the log against the federal reimbursement worksheet to ensure the proper accounting for all payments. The department will also remind staff to record payments in contract logs as soon as loans are disbursed.

The department will continue to review financial statements by utilizing the SCO checklist to assure accuracy, and will consider generally accepted accounting principles adjustments as they relate to this fund in the review process. Further, the department will identify loans disbursed after the May interest-billing date to make sure that interest is properly accrued for these loans. Finally, department staff will attend training to ensure that loan activity is accounted for in accordance with the CALSTARS Procedures Manual.

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## SECRETARY OF STATE

Reference Number: 2001-19-2

### CONDITION

The Secretary of State's Office did not exercise adequate control over its cash account during fiscal year 1999-2000. As a result, it did not have an accurate and complete record of its cash transactions for the year. In particular, we observed the following:

- The Secretary of State's Office did not promptly remit cash receipts to the State Treasurer's Office (Treasurer's Office). For the 12 receipts we reviewed, it remitted nine items (\$120,500 of \$125,300) between 14 to 76 days after the date of receipt, all of which were beyond the required timelines. For the remaining three items, totaling \$4,800, we were unable to calculate the number of days between receipt and remittance because the Secretary of State's Office was not able to provide the date of receipt.
- It did not prepare required monthly bank reconciliations during fiscal year 1999-2000. In addition, while it attempted to reconcile its general ledger cash balance to the State Controller's Office (Controller's Office) balance as of June 30, 2000, it could not explain a difference of \$189,000. To close its books for fiscal year 1999-2000, it adjusted its cash balance to agree with the Controller's Office balance without determining the reason for the difference. During the audit, we noted that the Secretary of State's Office did not prepare monthly bank reconciliations for fiscal year 2000-01. Following the conclusion of the audit, the Secretary of State's Office informed us that it had not completed the reconciliations for each of the months of fiscal year 2000-01 until the week of July 13, 2001.
- It did not take action to cancel or send stop payment requests to the Treasurer's Office for 251 general fund checks, totaling \$9,900, dated after January 1, 1999, and over one year old as of June 30, 2000, that its records indicated were outstanding. In addition, its records show a revolving fund check dated June 30, 2000, for \$50,000 was outstanding for at least 10 months. Staff of the accounting unit were not aware the check had not cleared until we called it to their attention and could not explain why it had not cleared.

Unless the Secretary of State's Office maintains necessary controls over its cash, reconciles its cash balance each month, identifies reconciling items and errors appropriately, and monitors outstanding checks, it cannot ensure that cash balances are accurate or that cash assets are properly safeguarded.

## **CRITERIA**

The State Administrative Manual, Section 8091, requires state agencies to remit to the State Treasury, regardless of the amount, all moneys determined to be revenue, reimbursements, abatements, and operating revenue within 30 days following the date collected, unless more frequent remittances are required. Further, accumulated deposits of \$25,000 must be remitted as soon as possible, but not later than the first day of the week following the accumulation.

Sections 7967 and 8060 require state agencies to reconcile each month their end of month bank and centralized State Treasury System account balances.

Section 8042 states that office revolving fund and agency checks issued on or after January 1, 1998, have a one-year period of negotiability. Office revolving fund checks uncashed or unclaimed for more than one year will be canceled and the amount of such checks will be remitted to a separate account in the fund from which they were drawn. Furthermore, Section 8045 requires state agencies to send stop payment requests to the Treasurer's Office one week before the stale date of all uncashed agency checks.

## **RECOMMENDATIONS**

We recommend that the Secretary of State's Office take the following action:

- Remit cash receipts when they reach \$25,000, or at least weekly.
- Prepare monthly bank reconciliations promptly.
- Appropriately monitor and cancel all stale-dated checks.
- Consider requesting assistance from the Department of Finance's Fiscal Systems and Consulting Unit to strengthen and improve its controls over its accounting for cash.

## **OFFICE'S VIEW AND CORRECTIVE ACTION PLAN**

The Secretary of State's Office concurs with our finding and indicates that it believes that the problems were related to its new accounting system. Specifically, it believes conversion to the new system and coding errors resulted in the \$189,000 discrepancy between the Controller's Office records and the Secretary of State's Office records for which it has no documentation identifying the specific cause. Further, it states that problems with coding of revenue delayed remittances to the Treasurer's Office. Currently, it indicates that it has addressed the conditions described above by improving its reporting system, remitting cash receipts to the Treasurer's Office every other day, and reconciling its bank account monthly. Also, it reports that it is in the process of clearing or canceling stale-dated checks.



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## **SECRETARY OF STATE**

Reference Number: 2001-19-3

### **CONDITION**

The Secretary of State's Office failed to adequately segregate duties in its accounting unit. Specifically, one employee authorized disbursements and controlled blank check forms. Two other employees prepared checks, compared checks with supporting documentation, and controlled blank check forms. Finally, another employee originated billing information, prepared invoices, maintained accounts receivable ledgers, determined accuracy of invoices, authorized adjustments, and handled disputed items. Lack of adequate segregation of duties may allow errors and irregularities to go undetected.

### **CRITERIA**

The California Government Code, Section 13403, requires state agencies to effectively maintain internal accounting and administrative controls. Such controls include segregation of duties appropriate for proper safeguarding of state agency assets. Specifically, the State Administrative Manual (SAM), Section 8080, provides that the same person will not perform more than one of the following types of duties:

- Authorizing disbursements
- Preparing checks
- Comparing checks with authorizations and supporting documentation
- Reconciling bank accounts and posting the general ledger or any subsidiary ledger affected by cash transactions
- Initiating or preparing invoices

In addition, persons comparing checks to supporting documentation will not have access to or control blank check stock.

### **RECOMMENDATION**

We recommend that the Secretary of State's Office appropriately segregate duties in its accounting unit to safeguard assets and ensure accurate record-keeping.

## **OFFICE'S VIEW AND CORRECTIVE ACTION PLAN**

The Secretary of State's Office concurs with our finding. It indicates that the accounting unit has reorganized the job duties to ensure that no one person performs more than one of the duties as outlined in the SAM.

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### **DEPARTMENT OF GENERAL SERVICES DEPARTMENT OF DEVELOPMENTAL SERVICES**

Reference Number: 2001-19-4

#### **CONDITION**

The Department of General Services (General Services) plays an important role in maintaining complete and accurate inventory records. Its Real Estate Services Division maintains the Statewide Real Property Inventory for state agencies. Similar to other agencies, it also buys and sells property that must be both recorded in the Statewide Real Property Inventory and reported to the State Controller's Office (Controller's Office). Its Office of Fiscal Services (Fiscal Services) maintains the general ledger for general fixed assets it reports to the Controller's Office. In addition, Fiscal Services is responsible for annually reconciling its records with the Statewide Real Property Inventory. If errors or inaccuracies are found, Fiscal Services is responsible for correcting its records and for informing the Real Estate Services Division of any errors in the Statewide Real Property Inventory that relate to General Services.

For fiscal year 2000-01, General Services did not ensure that adjustments that it identified to the Statewide Real Property Inventory and its general ledger were recorded on time. Specifically, although Fiscal Services conducted the annual reconciliation, it did not record adjustments to its general ledger for items it had previously identified for adjustment. In addition, although Fiscal Services informed the Real Estate Services Division of errors in the Statewide Real Property Inventory, the Real Estate Services Division did not correct the Statewide Real Property Inventory. As a result, Fiscal Services has not made adjustments of nearly \$15 million in its general ledger and the Real Estate Services Division has not adjusted approximately \$80 million in the Statewide Real Property Inventory. We reported a similar condition for fiscal year 1998-99. In its corrective action plan, General Services planned to annually reconcile its internal real property records to the Statewide Real Property Inventory.

Also, the Department of Developmental Services' (Developmental Services) financial services branch did not reconcile the amount reported to General Services for the Statewide Real Property Inventory with the information it reported to the State

Controller's Office (Controller's Office) in its Statement of Changes in General Fixed Assets, which is used in the State's financial statements. For fiscal year 2000-01, we reviewed the real property listing that Developmental Services maintains for the Sonoma Developmental Center (center) and compared it to the Statewide Real Property Inventory. Although Developmental Services reconciles the list of structures and improvements, the valuation amounts reported to General Services and to the Controller's Office for these properties differed. Specifically, we found that the amount for structures and improvements Developmental Services reported to the Controller's Office on the Statement of Changes in General Fixed Assets is more than \$27 million greater than the amount on the Statewide Real Property Inventory.

Unless departments report complete and accurate information to the Controller's Office and General Services' Real Estate Services Division, the State's financial statements will be misstated and the Statewide Real Property Inventory will be incomplete and inaccurate.

## **CRITERIA**

In our review of the State's General Fixed Assets, we determined that the following compliance requirements relate to General Services and Developmental Services:

The California Government Code, Section 11011.15, requires each state agency, including General Services, to furnish General Services with a record of each parcel of real property that it possesses and to update its real property holdings by July 1 of each year. It also requires General Services to maintain a complete and accurate inventory of all real property held by the State. General Services includes the departments' information in the Statewide Real Property Inventory.

Additionally, the State Administrative Manual, sections 7463, 7977, and 8660, requires agencies to report to the Controller's Office in a Statement of Changes in General Fixed Assets all additions and deductions to real property funded by governmental funds. The Controller's Office includes this information in the State's financial statements.

Further, the Department of Finance (Finance) issued directives in August 1999 and July 2000 requiring agencies to evaluate the risk of an incomplete inventory and to reconcile the amounts reported in the Statewide Real Property Inventory with the Statement of Changes in General Fixed Assets. Finance also required agencies to periodically reconcile their real property inventories to ensure the inventories are complete and accurate.

## **RECOMMENDATIONS**

General Services should ensure that it promptly records adjustments it identifies to the Statewide Real Property Inventory and its Statement of Changes in General Fixed Assets.

Developmental Services should annually reconcile amounts it reports in the Statewide Real Property Inventory to its Statement of Changes in General Fixed Assets.

## **DEPARTMENTS' VIEWS AND CORRECTIVE ACTION PLANS**

General Services agrees that it needs to ensure that adjustments to the Statewide Real Property Inventory and its general ledger are recorded promptly. General Services indicates it has completed posting journal entry adjustments for the fiscal year ended June 30, 2001, to the general ledger for the fixed assets account. Additionally, in March 2002, it plans to implement procedures to reconcile monthly the general ledger to the Statewide Real Property Inventory.

Developmental Services concurs with our finding and indicates that it will review the values reported by the Sonoma Developmental Center to determine the correct balance to be reflected on the Statement of Changes in General Fixed Assets it submits to the Controller's Office. Further, once this process is complete and appropriate adjustments have been made, Developmental Services will implement procedures to ensure that the annual Statewide Real Property Inventory prepared by the Sonoma Developmental Center is forwarded to Developmental Services' Developmental Center Division for review and approval of any necessary adjustments to the General Fixed Assets Account Group. Developmental Services states that the procedures implemented at the Sonoma Developmental Center will be followed at the other developmental centers in the State before the next fixed asset reporting period.

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## **DEPARTMENT OF GENERAL SERVICES**

Reference Number: 2001-19-5

## **CONDITION**

The Department of General Services (General Services), Office of Fiscal Services, maintains the accounting and financial records for construction projects managed by General Services' Real Estate Services Division. At the end of the fiscal year, the Office of Fiscal Services reports in summary the beginning balance, additions, deductions, and ending balance of projects as "construction in progress" for inclusion in the State's financial statements.

For the fiscal year ending June 30, 2000, we reported that the Office of Fiscal Services' general ledger account for construction in progress did not reconcile with its subsidiary records. At that time, the general ledger balance was approximately \$1.7 billion while a preliminary project listing totaled almost \$2.1 billion, a difference of \$400 million. In its corrective action plan, General Services stated that it planned to develop written procedures to reconcile its file of open projects with its construction-in-progress general ledger account. It also planned to develop procedures to identify additions and deductions to construction in progress. General Services expected to have the procedures to begin a reconciliation process completed by May 2001. Although it has developed procedures to identify additions and deductions to construction-in-progress, General Services has yet to develop procedures to reconcile its general ledger balance to its file of projects in progress. Furthermore, as of January 2002, it had only identified additions and deductions to construction in progress for one month, February 2001. Although General Services has reconciled a large amount of the difference between the general ledger balance and the preliminary project listing, there still existed a difference of over \$23 million. Unless the subsidiary records support the general ledger balance, General Services has less assurance that the amounts in the State's financial statements are correct.

## **CRITERIA**

The State Administrative Manual, Section 7900, says that the accuracy of a number of the accounting records of an agency may be proved partially by making reconciliations and verifications. Likewise, a good internal control system dictates that subsidiary records support general ledger balances.

## **RECOMMENDATION**

To ensure proper year-end reporting of construction-in-progress balances in the State's financial statements, General Services should develop procedures to reconcile its general ledger balance with its subsidiary records. Further, it should continue to identify current-year additions and deductions to construction in progress for inclusion in the State's financial statements.

## **DEPARTMENT'S VIEW AND CORRECTIVE ACTION PLAN**

General Services agrees with our finding and recommendation. It plans to continue identifying additions and deletions to its construction-in-progress account on a monthly basis. In addition, General Services will direct staff to develop a process to reconcile its file of active projects with the general ledger construction-in-progress account. It expects to implement this reconciliation process by July 31, 2002.

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## **VARIOUS STATE DEPARTMENTS**

Reference Number:

2001-19-6

### **CONDITION**

State departments do not always report their employees' taxable benefits and business expense reimbursements. Federal and state tax laws require that employers report income and related tax for payments other than regular wages, including benefits and business expense reimbursements. These benefits—cash, property, or services received in addition to regular pay—are reportable as taxable income unless specifically excluded in Internal Revenue Service (IRS) regulations. Examples of such taxable reimbursements include moving and relocation expenses, mileage compensation for commuting or personal travel between home and office when employees must work overtime (overtime or callback mileage), and payment for employees' meals when they must work overtime or travel for less than 24 hours without lodging.

The State Controller's Office (Controller's Office) informs state departments through its Payroll Procedures Manual and its Payroll Letters of the IRS requirements for reporting taxable benefits and taxable business expenses. These employee benefits and business expense reimbursements must then be included in a report to the Controller's Office by the 10<sup>th</sup> of the month following the month in which the payments were made. The Controller's Office then calculates and deducts the required taxes.

Despite these requirements, some departments do not always ensure that all employees' taxable benefits or taxable business expense reimbursements are being reported to the Controller's Office. We reviewed the reporting of employee taxable benefits and reimbursements at certain state departments for fiscal year 2000-01, including approximately 115 travel expense claims at each entity to verify that employee taxable reimbursements were properly reported. However, not all of the travel expense claims we reviewed had taxable benefits claimed.

One of these state departments—the Managed Risk Medical Insurance Board (board)—did not always ensure it met the reporting requirements the Controller's Office described. The Office of Statewide Health Planning and Development processes travel expense claims for the board and on its behalf reports employees' taxable benefits and business expense reimbursements to the Controller's Office. The table shows the total number of travel expense claims with reportable items that we reviewed and the number of items not reported to the Controller's Office.

We reported similar concerns for fiscal year 1999-2000 at seven other departments. Three of these departments have established and implemented internal procedures for reporting taxable benefits to the Controller's Office. Based on our review of 167 of its travel expense claims, one of these departments—the Department of Parks and

Recreation—appears to report correctly to the Controller’s Office; however, it has not yet developed written procedures to ensure that it consistently and correctly reports taxable benefits. Furthermore, as we reported in fiscal years 1998-99 and 1999-2000, the State Water Resources Control Board has not implemented any internal procedures for reporting personal use of state vehicles to the Controller’s Office. Finally, while two departments—the Department of Health Services and the Department of Rehabilitation—have developed internal procedures for reporting taxable benefits, they have not accurately reported taxable benefits to the Controller’s Office. The total number of travel expense claims with reportable items that we reviewed and the number of items not reported to the Controller’s Office are shown in the table below.

**Table**

***Reportable Items Reviewed That Were Not Reported to the Controller’s Office in Fiscal Year 2000-01***

State Agency	Total Number of Travel Expense Claims With Reportable Items Reviewed	ITEMS NOT REPORTED	
		Callback Mileage	Meals for Less Than 24-Hour Travel/Overtime Meals
Managed Risk Medical Insurance Board	19	5	6
Department of Health Services	14	1	4
Department of Rehabilitation	16	N/A	4
<b>TOTALS</b>	49	6	14

N/A: None included in travel expense claims reviewed.

Note: Some travel expense claims contained more than one type of reportable item.

When state departments do not properly report their employees’ taxable benefits and business expense reimbursements, the Controller’s Office cannot calculate and withhold the related tax, as required by federal and state laws and regulations.

**CRITERIA**

The Controller’s Office Payroll and Procedures Manual, sections 120 through 170, provides procedures for reporting to the Controller’s Office taxable benefits and business expense reimbursements provided to state employees. These procedures are based on federal and state tax laws. The following benefits and payments included in this manual relate to our testing of agency compliance:

- Section 130.1.2 states that reimbursement to employees for daily commuting expenses, such as for expenses from commuting or personal travel between home and office, is considered taxable income. This would include callback and overtime mileage.

- Section 143.3 states that overtime meal compensation is reportable and taxable income.
- Section 145.1.2 states that meal reimbursement for less than 24-hour travel without lodging is taxable income. Simply stated, if an employee receives reimbursement for meals during travel in which there was no overnight stay, this reimbursement is taxable income.

## **RECOMMENDATION**

To ensure proper reporting, all state departments should ensure that they have procedures implemented to properly report taxable benefits and taxable employee business expense reimbursements. In addition, the Managed Risk Medical Insurance Board should request a copy of the report of taxable benefits that the Office of Statewide Health Planning and Development submits to the Controller's Office on its behalf to ensure that the report has been submitted.

## **DEPARTMENTS' VIEWS AND CORRECTIVE ACTION PLANS**

The Managed Risk Medical Insurance Board (board) agrees with our finding. The board states that the Office of Statewide Health Planning and Development has corrected the errors found during the testing and provided copies of reports submitted to the Controller's Office. Also, the board indicates that the Office of Statewide Health Planning and Development has already implemented procedures and trained staff to ensure that taxable benefits and employee business expenses are reported to the Controller's Office monthly.

The Department of Parks and Recreation agrees with our finding. It indicates that it is currently developing procedures to ensure proper reporting of taxable benefits and business expenses to the Controller's Office.

The State Water Resources Control Board agrees with our finding. It states that it is in the process of establishing procedures to ensure the taxable amounts for personal use of state vehicles are reported to the Controller's Office.

The Department of Health Services agrees with our finding. The department has corrected the errors found during the testing and reported them to the Controller's Office. In addition, the department indicates it now has procedures in place for reporting of taxable benefits and has conducted training to ensure future reporting to the Controller's Office is systematic and complete.

The Department of Rehabilitation agrees with our finding. It states that it has implemented written procedures to ensure the capture and reporting of taxable benefits and reimbursements for proper reporting to the Controller's Office. Also, it indicates it has corrected its records and reported benefits and reimbursements previously overlooked to the Controller's Office.



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## **DEPARTMENT OF PERSONNEL ADMINISTRATION**

Reference Number: 2001-19-7

### **CONDITION**

In addition to the room rate, hotel and motel operators in California charge a transient occupancy tax ranging from 6 percent to 12 percent, depending on the location. Using the state transient occupancy tax waiver form developed by the Department of Personnel Administration (Personnel Administration), a state employee may request that the hotel or motel operator waive the occupancy tax. However, as stated on the form, hotel and motel operators are advised that their participation is strictly voluntary.

State departments inform employees of the existence of the form but may not require the employees to inquire about the acceptance of the form when making reservations or checking into hotels and motels. However, departments do not have systems in place to determine whether their employees request the waiver, or if the operator grants or denies the waiver. Unless they have a system in place to ensure that employees request the tax waiver, departments may be incurring more travel expenses than are necessary.

### **CRITERIA**

The State Administrative Manual, Section 710, states that lodging establishments may waive the transient occupancy tax if an employee shows proof that he or she is a state employee on official state business. The waiver is at the option of the lodging establishment.

### **RECOMMENDATION**

Personnel Administration should consider alternatives for improving the use of the waiver form by state employees. For example, it should consider establishing a procedure to ensure that state employees request the waiver and that departments monitor employee use of the waiver form. In particular, Personnel Administration could modify the standard travel expense claim to include a box for state employees to check, indicating whether the employees requested the waiver. Alternatively, procedures for filing travel expense claims could be modified to require employees to include the denied waiver form with their travel expense claims indicating that they requested the waiver but it was denied. State departments could then monitor travel expense claims to ensure their employees request the waiver.

## **DEPARTMENT'S VIEW AND CORRECTIVE ACTION PLAN**

Personnel Administration concurs with the facts of the finding and has indicated that, on the next revision of the travel expense claim form, it will consider adding a box for employees to check, indicating whether the employees requested the waiver. In addition, Personnel Administration explains that it developed the exemption form in response to state departments' inquiries regarding the tax-exempt status of employees traveling on state business. Further, when it developed the tax waiver form, the State's policy extended only to making the form available and notifying state departments that they may distribute the form to their employees and that the waiver was not mandatory on the part of hotel and motel operators. In addition, Personnel Administration states that the tax waiver has never been considered a viable method of controlling or limiting lodging expenses.

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## **DEPARTMENT OF MENTAL HEALTH DEPARTMENT OF HEALTH SERVICES**

Reference Number: 2001-19-8

### **CONDITION**

During fiscal year 2000-01, two state departments involved in the processing of payments associated with the federal Medical Assistance Program (Medicaid) did not always minimize the number of days elapsing between the disbursement of state funds and the receipt of federal funds for reimbursement of costs incurred. As a result, the State missed opportunities to earn interest on funds that should have been in its accounts. Specifically, we estimate that the State lost about \$170,000 in interest because prompt federal reimbursements were not obtained for five Medicaid claim schedules for mental health services and related administrative costs (mental health claims) totaling \$60 million. For these five mental health claims, the Department of Mental Health (Mental Health) and the Department of Health Services (Health Services) took up to 36 days to process the claims and to obtain federal reimbursing funds after using State General Fund money to pay them. During fiscal year 2000-01, Mental Health and Health Services paid about \$530 million in mental health claims.

### **CRITERIA**

Sound cash management techniques require the State to take full advantage of its opportunities to earn interest on funds in its accounts by minimizing the number of days that elapse between the disbursement of state funds for federal program purposes and the receipt of federal reimbursing funds.

## **RECOMMENDATION**

Health Services and Mental Health should jointly evaluate their cash management systems with the goal of reducing the number of days that elapse between the payment of mental health claims using State General Fund money and the receipt of federal reimbursing funds.

## **DEPARTMENTS' VIEW AND CORRECTIVE ACTION PLAN**

Health Services is reviewing internal procedures to determine the reasons for delays in claiming federal reimbursement for Medicaid claims for mental health services. Health Services will work with Mental Health to jointly evaluate each department's cash management system, with the goal of reducing the number of days elapsed between payment of mental health claims using State General Fund money and the receipt of federal reimbursing funds.

Mental Health states that it will work with Health Services to make any changes in its current process that would allow Health Services to draw federal funds more timely.

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## **DEPARTMENT OF HEALTH SERVICES**

Reference Number: 2001-19-9

## **CONDITION**

The Department of Health Services (department) contracts with a service provider to process and summarize electronically billions of dollars annually in claims from physicians, hospitals, pharmacies, and other health care providers under the Medi-Cal program. The contract requires the service provider to contract in turn with an independent certified public accounting (CPA) firm to perform an annual audit of general and application controls on the service provider's electronic data processing system and on its quality control efforts. This contract is subject to the department's approval, and the department specifies the functions to be audited in any given year. The purpose of the audit is to provide the department with some assurance that the service provider has systems and controls in place to ensure that it is appropriately processing the claims and accurately summarizing and reporting the financial information. The service provider's data are the basis for the payments of these claims and the reporting of the information in both the State's general purpose financial statements and in required reports to the federal government, which funds part of the payments through the Medical Assistance Program grant.

The independent CPA's report on the service provider for 2001 did not comply with contract requirements. In particular, the CPA did not follow auditing standards in executing its work or in reporting the results of its work. Auditing standards require the auditor to state explicitly what standards were followed in performing the audit work and to issue a formal report in accordance with the specified auditing standards. Instead, although the CPA's engagement letter for the work twice characterizes the planned work as an audit, the CPA has indicated informally that it followed American Institute of Certified Public Accountants consulting standards, which differ from auditing standards. Consulting services are nonattest services that involve advice or recommendations to a client. The CPA's report itself, however, has no indication of what standards the CPA followed. It also has no opinion and no clear indication, such as an authorized signature for the CPA firm or even the firm's letterhead, that the CPA firm is the author of the report. As a result, the report does not provide the department with the necessary assurances about the controls and quality assurance procedures of the service provider.

Further, given the magnitude of the transactions the service provider processes and their impact on the State's financial statements and federal reports, we believe the department should consider amending its contract with the service provider to require an audit in conformity with Statement of Auditing Standards Number 70 (SAS 70), "Service Organizations," which would report on controls placed in operation and results of tests of operating effectiveness. Such an audit would disclose whether the auditor believes the service organization's controls are suitably designed to achieve specified control objectives, whether they had been placed in operation as of a specific date, and whether the controls that were tested were operating with sufficient effectiveness to provide reasonable assurance that the related control objectives were achieved during the period specified.

## **CRITERIA**

The contract between the department and its service provider requires that the service provider contract in turn with an independent CPA firm to perform an electronic data processing audit of general and application controls on the service provider's system for processing Medi-Cal claims and quality control efforts, with the department responsible for specifying the functions to be audited for any given period. This contract between the service provider and the CPA firm is subject to the department's approval.

Generally accepted auditing standards require that the auditor issue a formal report that specifies the standards under which the audit is conducted and that is in accordance with the specified standards.

## **RECOMMENDATIONS**

To ensure that it is receiving the appropriate level of assurance about controls over the processing and reporting of Medi-Cal claims, the department should do the following:

- Before approving the contract between the service provider and the independent CPA firm, carefully review the contract provisions to determine that all elements of the audit requirements are properly specified, including a clear statement of which auditing standards the CPA will follow when conducting the audit.
- Review for compliance with contract provisions the engagement letter in which the independent CPA specifies, among other elements, the standards the firm will follow when conducting the audit.
- Review the audit report for compliance with contract deliverables and for all necessary elements, including a formal report in accordance with specified auditing standards on the results of the work performed and evidence of authorship of the report, such as an authorized signature of the CPA firm.

Further, the department should consider revising its contract with the service provider to specify that an audit in conformity with SAS 70, as described above, be performed.

## **DEPARTMENT'S VIEW AND CORRECTIVE ACTION PLAN**

The Department of Health Services generally agrees with our finding and recommendations and has indicated that it will incorporate our recommendations in its activities for the 2002 and subsequent audits. It has indicated that it will revise the contract to require that SAS 70 requirements, as amended, be followed for the 2002 audit. However, although it agrees that the CPA did not perform an audit, it believes that the CPA's work met the contractual requirements specifying that the scope of the work is to be determined by the department. Further, the department believes that its own monthly quality control review function and its internal audits have provided adequate oversight of the service providers' activities.

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## **CALIFORNIA DEPARTMENT OF TRANSPORTATION**

Reference Number: 2001-19-10

### **CONDITION**

The California Department of Transportation (Caltrans) has not always maintained accurate leave balance records for its employees. For the last several years, Caltrans has been working to address its high rate of incorrect leave balances, including instances of negative balances. In response to these problems, Caltrans performed a department-wide audit to reconcile and confirm balances for all of its employees.

We reviewed the leave balances for 40 employees from the three timekeeping systems that Caltrans maintains to report daily hours worked and leave used. Caltrans uses two different automated timekeeping systems: the Time Reporting System (TRS) that includes approximately 67 percent of Caltrans' employees and the Transportation Operations and Project Support System (TOPSS), totaling another 23 percent of the employees. In addition, 10 percent of employees use a manual timekeeping system. According to its chief of the Office of Transactions Services, in fiscal years 1999-2000 and 2000-01, Caltrans transitioned to the California Leave Accounting System (CLAS) for leave balance purposes. Caltrans transfers or manually enters leave used based on the automated and manual timekeeping information systems to the CLAS. We compared the leave balances we calculated to the leave balances in the CLAS as of May 2001. Our calculations were based on available records, which were not always complete.

Of the 40 employees we reviewed, 9 had leave balance differences between the CLAS and our calculation of 20 or more hours for either sick leave or vacation. For example, one TRS employee we reviewed had a vacation balance in the CLAS of 114 hours less than we calculated. The personnel specialist could not provide an explanation for this difference. In addition, the leave hours used for two TOPSS employees we tested were not entered into the CLAS until we brought it to Caltrans' attention because the personnel specialist did not add the employees to the CLAS. These employees' leave records went unreported for 17 months and 6 months, respectively. Also, two of the seven employees reviewed on the manual timekeeping system had vacation or sick leave balance differences between the CLAS and our calculation ranging from 31 to 36 hours. For these two employees, the time sheets clearly showed that leave had been used, but the usage was not posted to the CLAS. The records for two other employees on the manual timekeeping system were so incomplete as to make calculations of approximate leave balances impossible.

The table below shows the number of employees we reviewed for each timekeeping system and the number of employees with vacation or sick leave balance differences greater than 20 hours.

**Table**

***Leave Balances Reviewed That Had Differences of 20 or More Hours***

<b>Timekeeping System</b>	<b>Total Number of Employees Reviewed</b>	<b>Number of Employees With Vacation or Sick Leave Balance Differences of 20 or More Hours</b>
Time Reporting System (TRS)	25	3
Transportation Operations and Project Support System (TOPSS)	8	2
Manual time sheets	7	4
<b>TOTALS</b>	<b>40</b>	<b>9</b>

Based on interviews with Caltrans' personnel, contributing factors for these differences include high turnover of personnel specialists, high workloads, greater risk of error from manually entering leave information for employees using manual time sheets, and problems encountered when electronically transferring data from the TRS to the CLAS. Unless Caltrans maintains and documents accurate and complete timekeeping and leave balance records, its employees may receive more or less leave compensation than they have earned.

## **CRITERIA**

The California Government Code, Section 13401(b)(1), states that each state agency must maintain effective systems of internal accounting and administrative control as an integral part of its management practices. In addition, Section 13401(b)(2) states that each state agency will evaluate its systems of internal accounting and administrative control on an ongoing basis and, when detected, weaknesses must be promptly corrected. Finally, Section 13401(b)(3) states that all levels of management of the state agency must be involved in assessing and strengthening the systems of internal accounting and administrative control to minimize fraud, errors, abuse, and waste of government funds.

## **RECOMMENDATION**

Caltrans should ensure that it maintains and documents accurate leave balance records.

## **DEPARTMENT'S VIEW AND CORRECTIVE ACTION PLAN**

Caltrans concurs with our finding and recommendation. It states that it is currently implementing corrective action to ensure accurate leave records are maintained in its timekeeping systems and that leave is accurately reported to and reflected in the CLAS.

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## **DEPARTMENT OF FINANCE**

Reference Number: 2001-19-11

## **CONDITION**

The Department of Finance (Finance) does not effectively monitor variances between what departments budget and actually recover from the federal government for its share of statewide central service costs. As a result, Finance is not ensuring that the State maximizes federal reimbursement of these costs.

Of the five departments we sampled, we found that two did not receive any of the combined \$55,000 in statewide central service costs that they budgeted to recover from the federal government for fiscal year 2000-01. In October 2001, Finance sent an inquiry letter to one of these departments because it had not transferred budgeted recoveries of central service costs for at least a year. In December 2001, Finance sent letters to an additional 66 state departments that did not fully recover the budgeted federal portion of central service costs for fiscal years 1996-97 through 2000-01. The two departments in our sample each responded that they were unable to bill the federal government for these central service costs because they had not developed indirect cost rate proposals.

Two additional departments in our sample did not remit to the General Fund budgeted recoveries of central service costs of \$432,000 and \$22,000 for fiscal year 2000-01. In its January 31, 2002, response to Finance's inquiry, one department indicated that it recovered an unspecified amount of the \$432,000 in budgeted central service costs from the federal government but had not transferred those recoveries to the General Fund primarily because of cash flow and federal trust fund authority issues. As of February 7, 2002, Finance had not yet followed up with that department to determine the exact amount it had recovered from the federal government and when it planned to transfer the funds to the General Fund. The other department did not say in its January 29, 2002, response whether it had recovered central service costs for fiscal year 2000-01 from the federal government. Again, Finance has not yet followed up with that department to determine whether it recovered any central service costs from the federal government and, if so, how much and when those funds would be transferred to the General Fund.

Moreover, three of the departments in our sample also did not recover any of the combined \$77,000 they budgeted to receive from the federal government for fiscal year 1999-2000. If Finance had investigated these variances more thoroughly last year, it would have known that two of these departments lacked indirect cost rate proposals and could have advised these departments to prepare indirect cost rate proposals at that time. Thus, these departments could have begun recovering the federal share of statewide central service costs sooner.

## **CRITERIA**

The U.S. Office of Management and Budget Circular A-87, *Cost Principles for State, Local and Indian Tribal Governments* (OMB Circular A-87), Attachment E, Section D, requires state departments and agencies to prepare indirect cost rate proposals to recover indirect costs under federal awards. Indirect costs include the indirect costs originating in each department or agency carrying out federal awards and the costs of central governmental activities distributed through the statewide cost-allocation plan.

Additionally, the State Administrative Manual, Section 8755.1, states that each department receiving federal funds has the responsibility to file an indirect cost rate proposal with the federal government. Before submitting indirect cost rate proposals to the federal government, departments must send their proposals to Finance for review and approval.



## **RECOMMENDATIONS**

Finance should more effectively monitor variances between budgeted and actual recoveries of the federal share of statewide central service costs. This should include prompt follow-up with departments that do not substantially recover the budgeted federal portion of these expenses. Finally, except where prohibited by federal statute, Finance should ensure that departments prepare and submit indirect cost rate proposals to facilitate the recovery of the federal share of statewide central service costs.

## **DEPARTMENT'S VIEW AND CORRECTIVE ACTION PLAN**

Finance states that it currently monitors state departments recoveries of the federal share of statewide central service costs. Finance notes that for fiscal years 1996-97 through 2000-01, average recoveries were 88.2 percent of budgeted amounts. In its annual training classes, Finance will continue to emphasize that departments prepare indirect cost rate proposals and transfer federal funds to the General Fund on a timely basis. Finance will follow-up with those state departments not preparing indirect cost rate proposals and transferring federal funds to the General Fund.

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## **Compliance Issue Related to All Federal Grants**

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## IDENTIFYING PROGRAM EXPENDITURES

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Reference Number: 2001-12-7  
Federal Program: All Programs  
Category of Finding: Reporting

### CRITERIA

In our review of federal reports, we determined the following were among state and federal compliance requirements:

The U.S. Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations* (OMB Circular A-133), requires that the State prepare a schedule showing total expenditures for the year for each federal program. Further, OMB Circular A-133 requires that the State identify and audit all high-risk Type A federal programs, which are those exceeding .15 percent of total federal program moneys the State expends during the fiscal year. The California Government Code, Section 13300, assigns the Department of Finance (Finance) the responsibility for maintaining a complete accounting system to ensure that all revenues, expenditures, receipts, disbursements, resources, obligations, and property of the State are properly tracked and reported.

### CONDITION

Because of limitations in its automated accounting systems, the State has not complied with the provision of OMB Circular A-133 requiring a schedule showing total expenditures for each federal program. As a result, the schedule (beginning on page 127 shows total receipts, rather than expenditures, by program. Expenditure information is necessary to identify Type A programs. To ensure that we identified and audited all high-risk Type A programs, we reviewed accrual basis expenditures, which are identified manually, for all programs that we did not already plan to audit and that had cash receipts within 10 percent of the Type A program threshold. We identified three such programs. Our review of the expenditures of these programs showed that none of them exceeded the Type A threshold.

### RECOMMENDATION

As priorities and resources permit, Finance should modify the State's accounting system to separately identify expenditures for all major programs.

## **DEPARTMENT'S VIEW AND CORRECTIVE ACTION PLAN**

Finance has responded that although the State, on a statewide basis, reports federal receipt totals, each individual state entity reports expenditures by grant to its federal cognizant agency. Finance states that the State's accounting system will require substantial modification to compile expenditure information to meet all federal and state requirements. Because the State has limited resources, Finance has no plans at this time to enhance the State's accounting system or to implement a new system.

**Compliance and Internal Control Issues  
Related to Specific Grants Administered  
by Federal Departments**

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## **U.S. DEPARTMENT OF AGRICULTURE**

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Reference Number:	2001-1-1
Federal Catalog Number:	10.557
Federal Program Title:	Special Supplemental Nutrition Program for Women, Infants, and Children
Federal Award Numbers and Calendar Years Awarded:	7CA700CA7; 1999 7CA700CA7; 2000
Category of Finding:	Allowable Activities
State Administering Department:	Department of Health Services

### **CRITERIA**

Our review of the Special Supplemental Nutrition Program for Women, Infants, and Children (WIC Program) found the following compliance requirements related to allowable activities:

The Code of Federal Regulations, Title 7, Section 246.14(d), requires the prior approval from the United States Department of Agriculture's Food and Nutrition Service (FNS) for costs for automated data-processing systems. Further, under the FNS Handbook 901, Section 5000, the FNS has authorized state agencies administering the WIC Program to make data-processing acquisitions with a total project cost up to \$24,999 without prior approval. For data-processing acquisitions exceeding \$24,999, the WIC Program must obtain prior approval from the FNS before the expense is incurred.

### **CONDITION**

Although it has procedures in place to ensure that it obtains prior approval from the FNS for data-processing project costs exceeding \$24,999, the Department of Health Services (Health Services) does not always adhere to them. By not following FNS procurement procedures, Health Services increases the risk that the disbursement of WIC Program funds may be for unallowable purposes. For one of the two data-processing acquisitions that exceeded \$24,999, Health Services failed to obtain the required FNS approval before it incurred the expenses. Specifically, Health Services acquired automated data-processing materials with a total project cost of almost \$36,000 without first obtaining FNS approval for this acquisition.

## RECOMMENDATION

Health Services should ensure that it follows FNS procurement procedures and obtain approval before it incurs data-processing project costs exceeding \$24,999.

## DEPARTMENT'S VIEW AND CORRECTIVE ACTION PLAN

Health Services concurs with the finding. It stated that it has reviewed its procurement process and will implement changes to ensure appropriate approvals are obtained prior to incurring expenses. These changes include updating the routing of procurements for authorized signatures, providing comprehensive training to all contract staff, updating procurement procedures for requests for applications and proposals, improving tracking, and ensuring follow-up is maintained.

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Reference Number:	2001-2-2
Federal Catalog Number:	10.558
Federal Program Title:	Child and Adult Care Food Program
Federal Award Number and Calendar Year Awarded:	7CA300CA3; 2000
Category of Finding:	Allowable Costs and Cost Principles
State Administering Department:	Department of Education

## CRITERIA

Our review of the Child and Adult Care Food Program (food program) determined that the following federal requirement relates to allowable costs and cost principles:

The U.S. Office of Management and Budget Circular A-87, *Cost Principles for State, Local and Indian Tribal Governments* (OMB Circular A-87), provides the guidelines for determining allowable costs. OMB Circular A-87 states that for costs to be allowable under a federal award, costs must be necessary and reasonable for proper and efficient performance and administration of federal awards.

## CONDITION

The Department of Education (Education) overpaid a food program sponsor \$14,350 because it entered an incomplete claim adjustment into its claim payment system. Originally, the sponsor claimed 7,999 suppers on its initial meal reimbursement claim.

One month later, the sponsor submitted an adjustment claim showing the 7,999 meals as snacks; however, the sponsor left the suppers box on the claim form blank instead of writing in a zero. When Education entered the adjustment claim into its automated claim-processing system, it entered only the snack meal count, but did not revise the supper meal count to zero. Consequently, because Education's system does not adjust previously entered meal counts when no revised count is entered, Education did not recover the payment for the erroneously claimed suppers, resulting in a \$14,350 overpayment to the sponsor.

Additionally, this overpayment increased the sponsor's average monthly reimbursement, which Education uses when calculating the allowable cash advance. As a result, Education overpaid the cash advance to the sponsor by more than \$9,550. When we brought these overpayments totaling \$23,900 to Education's attention, it recovered the claim and advance overpayments from the sponsor.

When Education does not have adequate procedures to prevent errors while processing adjustment claims, it risks paying sponsors incorrect amounts. Education said it would eventually have detected and taken corrective action on this overpayment when it ran its annual exception report identifying sponsors who claimed certain types of meal reimbursement that the sponsor does not normally claim. Education stated that for these unusual claims, it follows up with the sponsor to determine whether the claim is valid and takes action to recover any overpayments.

## **RECOMMENDATIONS**

Education should improve its procedures for processing adjustment claims for the food program. Specifically, Education should improve its instructions to sponsors for completing meal-reimbursement claim forms and run exception reports more frequently to help detect inappropriate payments. Additionally, Education should instruct staff to compare the original and adjustment claims to ensure the appropriateness and completeness of the adjustment before entering the data in the system.

## **DEPARTMENT'S VIEW AND CORRECTIVE ACTION PLAN**

Education Child Nutrition Fiscal Services in their view has provided complete instructions to its sponsors detailing the procedures for filing adjustment claims when adjusting meal counts. Education has since added these instructions to the back of the reimbursement claim forms to further assist the sponsors.

Education is aware of the meal supper/supplement switch and has implemented new procedures when processing adjustment claims. Staff now pulls the original claim and compares it to the adjustment, highlighting all changes being made to the claim. When a discrepancy in the meal counts occurs, the sponsor is contacted for clarification and correction. As a second check, staff is running a monthly report of

meal counts to identify sponsors who have discrepancies in meal types claimed, specifically suppers and supplements. If a discrepancy occurs, sponsors are contacted by letter and required to submit an adjustment to correct the error.

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Reference Number: 2001-5-1  
Category of Finding: Eligibility  
State Administering Department: Department of Education

(See listing of the specific federal program details following the discussion of the issues below.)

## **CRITERIA**

Our review of the Special Milk Program for Children and the Summer Food Service Program for Children identified the following compliance requirements related to eligibility:

The Code of Federal Regulations, Title 7, Section 215.7, requires participants in the Special Milk Program for Children to submit written applications and, upon approval, enter into a written agreement with the State administering department. Furthermore, participants who wish to serve free milk must submit a free-milk policy statement to the administering department.

Additionally, the Code of Federal Regulations, Title 7, Section 225.6, requires participants in the Summer Food Service Program for Children to submit free-meal policy statements to the administering department. Further, Section 225.14 requires Summer Food Service Program for Children sponsors to be public or nonprofit private entities.

## **CONDITION**

The Department of Education (Education) could not demonstrate the eligibility for all participants we reviewed in the Special Milk Program for Children and Summer Food Service Program for Children. Of the 40 Child Nutrition Cluster sample items we tested, 20 related to the Special Milk Program for Children and Summer Food Service Program for Children. For these 20 sample items, Education was unable to locate the file for one of its Special Milk Program for Children sponsors. In addition, Education was unable to provide documents to show that four sponsors of the Special Milk Program for Children and one sponsor of the Summer Food Service Program for Children submitted the required free-milk or free-meal policy statements. Further, Education did not have documents in its files to verify the nonprofit status of one

Summer Food Service Program for Children sponsor. When it does not maintain complete participant files, Education cannot assure that it provides federal assistance only to eligible participants.

## **RECOMMENDATION**

Education should ensure that it receives and retains documentation demonstrating the eligibility of all participants in the Special Milk Program for Children and the Summer Food Service Program for Children.

## **DEPARTMENT'S VIEW AND CORRECTIVE ACTION PLAN**

Education has recognized that the former filing system was inadequate and has reorganized the Nutrition Services Division (NSD) file rooms into a secured central filing system. To ensure that files are kept in the file room, NSD has established a process to ensure that all files removed from the file room must be returned within 10 working days.

During the administrative review process, NSD staff will be reviewing the program files to ensure that all required eligibility documents have been filed. Updating of documents will also take place during this time.

### **U.S. DEPARTMENT OF AGRICULTURE**

Federal Catalog Number:	10.556
Federal Program Title:	Special Milk Program for Children
Federal Award Number and Calendar Year Awarded:	7CA300CA3; 2000
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Federal Catalog Number:	10.559
Federal Program Title:	Summer Food Service Program for Children
Federal Award Number and Calendar Year Awarded:	7CA300CA3; 2000
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Reference Number:	2001-13-2
Federal Catalog Number:	10.558

Federal Program Title: Child and Adult Care Food Program  
Federal Award Number and Calendar Year Awarded: 7CA300CA3; 2000  
Category of Finding: Subrecipient Monitoring  
State Administering Department: Department of Education

## **CRITERIA**

Our review of the Child and Adult Care Food Program (food program) determined that the following federal requirements relate to subrecipient monitoring:

The Code of Federal Regulations, Title 7, Section 226.6(l)(1)-(3), requires states to review newly participating sponsors with five or more child care facilities or adult day care facilities within the first 90 days of operation. Further, states must review independent centers, sponsors of centers, and sponsors of day care homes with up to 200 homes at least once every four years and review sponsors of day care homes with more than 200 homes at least once every two years.

## **CONDITION**

The Department of Education (Education) did not adequately fulfill its subrecipient monitoring responsibilities for the food program. Specifically, we reviewed seven new sponsors that Education approved to participate in the food program between July 1, 2000, and April 1, 2001, and found that Education had not conducted an administrative review for five sponsors within the first 90 days of operation. The reviews were from 5 to 11 months overdue. Education said an oversight caused these reviews to be late. When Education does not conduct timely reviews of its new sponsors, it cannot ensure that the sponsors began operations with the proper procedures in place to comply with federal food program regulations and administrative requirements.

Additionally, for its existing sponsors, Education could not locate 1 of the 40 sponsor review files that we selected to review. To validate whether Education reviewed the sponsor within the required time interval, the date of the last administrative review must be determined from the review file. However, because Education could not locate the file, we could not make this determination. When Education does not maintain adequate control over sponsor review files, it cannot demonstrate that it has reviewed sponsors within the required time interval.

## **RECOMMENDATIONS**

Education should establish procedures to ensure it reviews all new participating sponsors with five or more sites within the first 90 days of operation. Education

should also improve its file management procedures to ensure it can locate all its sponsor review files.

## **DEPARTMENT'S VIEW AND CORRECTIVE ACTION PLAN**

To ensure compliance with the regulatory requirement to perform an administrative review within 90-days of program implementation for each new sponsor who is approved with 5 or more sites, Education is implementing the following procedural changes:

1. It is now the responsibility of the Nutrition Services Division (NSD) Field Services Unit (FSU) to evaluate and approve all new applications. The appropriate Regional Manager will sign the approval. Upon approval, the new sponsor is added to a Nutrition Services Representative's caseload. The NSD Representative and the appropriate Regional Manager will be aware of the 90-day review requirement if the agency has 5 sites or more when approved.
2. During the approval process, the Regional Manager works with the NSD Representative to schedule the 90-day review. This scheduled date is noted on the approval checklist.
3. Education is requesting changes to the Child and Adult Care Food Program sponsor database to include posting the number of sites approved during the initial approval and the "scheduled date" for the 90-day review on the application approval log. Education is also requesting a programming change to add the scheduled 90-day review date into the review tracking system. When this is done, the FSU Manager will then receive a monthly report of scheduled reviews from these systems that will flag the up-coming 90-day reviews.
4. NSD representatives provide a monthly report to their Regional Manager on all scheduled review activities that can be used to cross-check to ensure review requirements are met.

Education Management will receive a quarterly report of administrative review activities including required 90-day reviews, dates scheduled and date conducted. This will allow Education Management to monitor review activities and take appropriate actions to ensure compliance with federal regulations.

Education consolidated its five nutrition program file rooms into one central file location and established a file clerk position as of August 2001. Education has developed new file protocols that only allow the file clerk into the file room and require Education personnel to sign for each file requested. The file clerk currently is performing file maintenance and reports weekly to division management on the process of rectifying filing errors.

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Reference Number:	2001-14-1
Federal Catalog Number:	10.557
Federal Program Title:	Special Supplemental Nutrition Program for Women, Infants, and Children
Federal Award Numbers and Calendar Years Awarded:	7CA700CA7; 1999 7CA700CA7; 2000
Category of Finding:	Special Tests and Provisions
State Administering Department:	Department of Health Services

## **CRITERIA**

Our review of the Special Supplemental Nutrition Program for Women, Infants, and Children (WIC Program) found the following requirement related to special tests and provisions:

The Code of Federal Regulations, Title 7, Section 246.19(b), requires the Department of Health Services (Health Services) to conduct monitoring reviews of each local agency at least once every two years. Local agencies include public and private nonprofit health or human services agencies that provide health services, either directly or through contracts. These monitoring reviews must examine several areas of the local agency, including its financial management system. Furthermore, Health Services must have a corrective action process that includes notifying local agencies of any deficiencies found during these reviews.

## **CONDITION**

Health Services did not ensure that the financial management systems of all local agencies were examined during monitoring reviews for fiscal years 1999-2000 and 2000-01. Nor did it always promptly notify local agencies of the deficiencies found during these reviews. As a result, Health Services cannot ensure that all local agencies are properly administering the WIC Program; at the same time, the risk that local agencies will not promptly correct deficiencies is increased.

During fiscal years 1999-2000 and 2000-01, Health Services did not ensure that the financial management systems for all 81 contracted local agencies were evaluated. To assist it in performing these evaluations, Health Services contracted with the State Controller's Office to review the financial management systems for some of the local agencies. Health Services intended to review the rest. Although Health Services and the State Controller's Office reviewed the financial management systems for a total of 67 local agencies, Health Services did not review



the remaining 14. In November 2000 Health Services revised its contract so that the State Controller's Office would review the financial management systems for half of all local agencies each year.

Further, Health Services did not always promptly notify local agencies of the deficiencies revealed during the monitoring reviews. According to program guidelines, Health Services generally issues a notification of findings (notifications) within 90 days after the program evaluation has occurred. However, of the 10 program evaluations we reviewed, Health Services failed to issue 4 notifications promptly. These notifications ranged from 15 to 64 days late.

## **RECOMMENDATIONS**

Health Services should ensure that all areas of the monitoring reviews are examined at least once every two years. It should also promptly notify local agencies about any deficiencies noted during these reviews.

## **DEPARTMENT'S VIEW AND CORRECTIVE ACTION PLAN**

Health Services concurs with the finding. Health Services has revised its contract with the State Controller's Office to ensure monitoring reviews of 40 to 41 providers annually. Further, Health Services has streamlined its procedures to ensure timely issuance of letters of findings to notify local agencies of deficiencies revealed during the monitoring reviews.

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Reference Number:	2001-14-2
Federal Catalog Number:	10.550
Federal Program Title:	Food Distribution
Year Awarded:	State fiscal year 2000-01
Category of Finding:	Special Tests and Provisions
State Administering Department:	Department of Education

## **CRITERIA**

Our review of the Food Distribution program identified the following compliance requirement relating to special tests and provisions:

The Code of Federal Regulations, Title 7, Section 250.19(b)(iii), requires the State to conduct on-site reviews of all food processors at least once every two years (except those that are multi-state processors) with no fewer than 50 percent being reviewed each year.

## **CONDITION**

The Department of Education (Education) did not fulfill its review responsibilities relating to its in-state food processors. During fiscal years 1999-2000 and 2000-01, Education failed to conduct on-site reviews of 9 of its 25 active in-state processors within the required two-year period. In addition, it reviewed only 24 percent of its active in-state processors during fiscal year 2000-01, rather than the required 50 percent. When it does not review in-state processors within the specified time periods, Education cannot assure that the in-state processors are meeting all Food Distribution program requirements.

## **RECOMMENDATIONS**

Education should ensure that it reviews all in-state food processors at least once every two years. It should also review at least half of the in-state food processors that are active for the Food Distribution program each fiscal year.

## **DEPARTMENT'S VIEW AND CORRECTIVE ACTION PLAN**

To immediately correct this compliance area, Education will review all twenty-two active in-state processors during the 2002 State Fiscal Year. Education has scheduled these reviews and is in the process of meeting this commitment.

In addition Education revised its processing review tracking system under guidance from the United States Department of Agriculture. The new system allows Education to schedule all necessary reviews, identify discontinued and multi-state processors, and monitor progress towards review closure.

Education Management will receive a quarterly report of processor review activities. This will allow Education Management to monitor compliance with the federal review requirements.

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Reference Number: 2001-14-6

Federal Catalog Number: 10.561

Federal Program Title:	State Administrative Matching Grants for Food Stamp Program
Federal Award Number and Calendar Year Awarded:	7CA400CA4; 2000
Category of Finding:	Special Tests and Provisions
State Administering Department:	Department of Social Services

## **CRITERIA**

Our review of the State Administrative Matching Grants for Food Stamp Program found the following compliance requirements related to the physical inventory of food coupons:

The Code of Federal Regulations, Title 7, Section 274.1(c)(1), requires the State to conduct an on-site review of each food stamp coupon issuer and storage site at least once every three years. Section 274.1(c)(2) allows the state agency to delegate this review responsibility to another unit of state government or contract with a certified public accounting (CPA) firm.

Additionally, Section 271.2 defines *state agency* to include the “counterpart local agencies that administer such assistance programs for the state agency.” This expanded definition of *state agency* allows the Department of Social Services (Social Services) to have its counterpart county agencies contract with another unit of county government or a CPA firm to have this review done.

Social Services’ Food Stamp Regulations, Section 63-601.272(c), makes the county welfare departments responsible for the required physical inventory review, specifying that the review may be performed by another unit of county government or contracted with an independent CPA firm.

## **CONDITION**

Social Services failed to ensure that all of the counties participating in the Food Stamps program obtained independent reviews. Of the 58 counties, 7 had the physical inventory review performed by their own welfare department, the same department that administers the Food Stamps program. As a result, Social Services cannot ensure that an independent review of food coupon inventories was completed for these counties. Additionally, Social Services did not require any of the counties to submit review reports for it to analyze; instead, Social Services depended on counties to self-report review findings, the date of the review, and who performed the review.

## **RECOMMENDATIONS**

Social Services should require all county welfare departments to have the required physical inventory review performed by an independent CPA firm or another unit of county government. In addition, Social Services should require all counties to submit complete review reports to it for review.

## **DEPARTMENT'S VIEW AND CORRECTIVE ACTION PLAN**

Social Services concurs. By April 1, 2002, Social Services will send a letter to the seven noncompliant counties requesting that effective July 1, 2001, and annually thereafter, they must enlist the services of a CPA or separate county audit agency to complete an independent audit of their bulk storage food stamp coupons. In this directive, Social Services will emphasize the requisites of an independent audit and ask these counties to provide Social Services with documentation that they have procured an independent audit of their bulk storage food stamp coupons for State fiscal year (SFY) 2001-02. Social Services will request that such documentation be sent to its Food Stamp Branch no later than May 10, 2002.

In addition to the current survey that Social Services issues to the 58 counties requesting information and documentation regarding completion of their food stamp bulk storage audits, Social Services will issue an All County Information Notice (ACIN) by June 30, 2002, emphasizing each county's responsibility to obtain annual, independent audits of their bulk storage services.

Finally, Social Services will select a random sample of at least seven counties each year beginning in SFY 2001-02, and request that these counties send copies of their food stamp bulk storage audit reports to Social Services. This selection process will be discussed in the ACIN referenced above. Social Services will review and follow-up on the annual survey results and on bulk storage audit reports to ensure that counties are in compliance with federal regulations.

**U.S. DEPARTMENT OF AGRICULTURE  
U.S. DEPARTMENT OF LABOR  
U.S. DEPARTMENT OF EDUCATION  
U.S. DEPARTMENT OF HEALTH AND HUMAN SERVICES**

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Reference Number: 2001-3-9  
Category of Finding: Cash Management  
State Administering Department: Department of Finance

(See listing of the specific federal program details following the discussion of the issues below.)

**CRITERIA**

We determined that the following requirements relate to compliance with the Cash Management Improvement Act:

The Code of Federal Regulations, Title 31, Section 205.15(a)(3)(4)(5), requires the State to submit an annual report to the U.S. Department of the Treasury accounting for the interest liabilities of the State's most recently completed fiscal year. This report must include the total federal and state interest liability for each program subject to the Cash Management Improvement Act Agreement (CMIA agreement) between the U.S. Department of the Treasury and the State, as well as the net total interest owed by the State or the federal government. Section 205.15(d) requires an authorized state official to certify the accuracy of the State's annual report.

Additionally, the CMIA agreement, Section 9.7.14, requires the State to calculate both state and federal interest liabilities on all administrative costs, including payroll and state operating costs, and to incorporate these calculations into the total interest liability information contained in the annual report.

**CONDITION**

The Department of Finance (Finance) requires state departments to report information related to the receipt and disbursement of federal funds of selected federal programs so that it can calculate interest liabilities under the CMIA agreement. However, we found that several departments submitted administrative cost worksheets for fiscal year 1999-2000 that included receipts or disbursements of federal funds that actually related to fiscal year 2000-01. Although Finance correctly omitted these transactions when calculating interest liabilities associated with administrative costs for fiscal year 1999-2000, it neglected to include these transactions in its fiscal year 2000-01

calculation. As a result of these omissions, Finance calculates that it overstated the State's net interest liability in the fiscal year 2000-01 annual report by nearly \$1.1 million.

## **RECOMMENDATIONS**

Finance should correct the errors contained in the State's fiscal year 2000-01 annual report by adjusting the interest liabilities of the affected programs in the fiscal year 2001-02 report. Finance should also ensure that interest liabilities contained in future annual reports are based on all receipts and disbursements of federal funds that occurred in the respective fiscal year.

## **DEPARTMENT'S VIEW AND CORRECTIVE ACTION PLAN**

Finance agrees with the finding. The overstated state interest liability will be reported and adjusted as a prior year adjustment in the fiscal year 2001-02 annual report that will be submitted to the U.S. Department of the Treasury in December 2002.

Finance states that it has implemented procedures that will accurately capture the interest liabilities for current year transactions that were reported in the previous fiscal year. Finance will also continue its ongoing efforts to reduce errors by improving internal procedures, analyzing the information reported by state departments, providing ongoing consultation and training, and annually reminding departments of their responsibilities.

### **U.S. DEPARTMENT OF AGRICULTURE**

Federal Catalog Number:	10.557
Federal Program Title:	Special Supplemental Nutrition Program for Women, Infants, and Children
Federal Award Number and Calendar Year Awarded:	7CA700CA7; 1999

### **U.S. DEPARTMENT OF LABOR**

Federal Catalog Number:	17.207
Federal Program Title:	Employment Service
Federal Award Number and Calendar Year Awarded:	T-0620599000; 1999

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Federal Catalog Number: 17.225  
Federal Program Title: Unemployment Insurance  
Federal Award Number and  
Calendar Year Awarded: No award number; 1999

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Federal Catalog Number: 17.246  
Federal Program Title: Employment and Training Assistance—  
Dislocated Workers  
Federal Award Number and  
Calendar Year Awarded: A-7351-9-00-87-50; 1999

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Federal Catalog Number: 17.250  
Federal Program Title: Job Training Partnership Act  
Federal Award Number and  
Calendar Year Awarded: A-7351-9-00-87-50; 1999

#### **U.S. DEPARTMENT OF EDUCATION**

Federal Catalog Number: 84.126  
Federal Program Title: Rehabilitation Services—Vocational  
Rehabilitation Grants to States  
Federal Award Number and  
Calendar Year Awarded: H126A000005; 1999

#### **U.S. DEPARTMENT OF HEALTH AND HUMAN SERVICES**

Federal Catalog Number: 93.558  
Federal Program Title: Temporary Assistance for Needy Families  
Federal Award Number and  
Calendar Year Awarded: G-9901CATANF; 1999

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Federal Catalog Number: 93.658  
Federal Program Title: Foster Care—Title IV-E  
Federal Award Number and  
Calendar Year Awarded: 9901CA1401; 1999

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Federal Catalog Number: 93.659  
Federal Program Title: Adoption Assistance  
Federal Award Number and  
Calendar Year Awarded: 9901CA1407; 1999

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Federal Catalog Number: 93.778  
Federal Program Title: Medical Assistance Program  
Federal Award Number and  
Calendar Year Awarded: 05-9905CA5048; 1999



**U.S. DEPARTMENT OF AGRICULTURE  
U.S. DEPARTMENT OF HEALTH AND HUMAN SERVICES**

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Reference Number: 2001-9-6  
Category of Finding: Suspension and Debarment  
State Administering Department: Department of Social Services

(See listing of the specific federal program details following the discussion of the issues below.)

**CRITERIA**

Our review of federal programs determined the following are compliance requirements related to suspension and debarment:

The Code of Federal Regulations, Title 45, Section 76.225, prohibits the State from knowingly doing business with any party that is suspended, debarred, or otherwise ineligible to participate in federal assistance programs. Further, Title 45, Section 76.510, requires the State to obtain certifications from participating organizations regarding debarment, suspension, ineligibility, and voluntary exclusion.

**CONDITION**

The Department of Social Services (Social Services) failed to require any of the counties receiving federal funds under the six federal programs we reviewed to submit the required suspension and debarment certification. Additionally, for the Adoption Assistance program, Social Services did not obtain certifications from two of the three contractors we reviewed from which Social Services contracted services totaling \$100,000 or more. Without obtaining the required certifications, Social Services runs the risk of unknowingly allowing suspended or debarred parties to participate in the federal programs. For the transactions we reviewed, we used an alternative test to determine that these subrecipients were not suspended or debarred.

**RECOMMENDATION**

Social Services should ensure that participants in its federal programs submit the required suspension and debarment certifications before Social Services approves their participation in a federal program.

**DEPARTMENT'S VIEW AND CORRECTIVE ACTION PLAN**

Social Services concurs. To address the requirement that it obtain "suspension and debarment certifications" from its contractors, Social Services' Contracts Bureau has implemented a procedure to obtain a "Certification Regarding Debarment,

Suspension, Ineligibility and Voluntary Exclusion-Lower Tier Transactions” for all federally funded agreements that total \$100,000 or more. This requirement was made a part of the standard language contained in Exhibit D for all Social Services contracts. Additionally, Social Services has revised its contracting process to include a random review of contract files during closeout and a checklist is being developed to enable the analysts to ensure that all necessary documents have been obtained. To address the requirement that it obtain similar certifications from the 58 County Welfare Departments, Social Services’ Fiscal Policy Bureau will issue a County Fiscal Letter by March 31, 2002, directing the counties to submit the required “suspension and debarment certifications” to Social Services annually, commencing with State fiscal year 2001-02.

**U.S. DEPARTMENT OF AGRICULTURE**

Federal Catalog Number:	10.551
Federal Program Title:	Food Stamps
Year Awarded	State fiscal year 2000-01

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Federal Catalog Number:	10.561
Federal Program Title:	State Administrative Matching Grants for Food Stamp Program
Federal Award Number and Calendar Year Awarded:	7CA400CA4; 2000

**U.S. DEPARTMENT OF HEALTH AND HUMAN SERVICES**

Federal Catalog Number:	93.558
Federal Program Title:	Temporary Assistance for Needy Families
Federal Award Number and Calendar Year Awarded:	G0001CATANF; 1999

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Federal Catalog Number:	93.658
Federal Program Title:	Foster Care—Title IV-E
Federal Award Number and Calendar Year Awarded:	0001CA1401; 1999

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Federal Catalog Number:	93.659
Federal Program Title:	Adoption Assistance
Federal Award Number and Calendar Year Awarded:	0001CA1407; 1999

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Federal Catalog Number:	93.667
Federal Program Title:	Social Services Block Grant
Federal Award Numbers and Calendar Years Awarded:	G-0101CASOSR; 2000 G-0001CASOSR; 1999 G-9901CASOSR; 1998

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Reference Number:	2001-13-1
Category of Finding:	Subrecipient Monitoring
State Administering Department:	Department of Health Services

(See listing of the specific federal program details following the discussion of the issues below.)

## **CRITERIA**

Our review of federal programs identified the following compliance requirements related to subrecipient monitoring:

The U.S. Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations* (OMB Circular A-133), describes the audit requirements for recipients of federal funds. Sections 200 and 320 require subrecipients spending \$300,000 or more annually in federal awards to submit audit reports to the State when the reports address findings related to the federal awards that the State administers. If a subrecipient's audit report contains no findings related to the federal awards administered by the State, the subrecipient must notify the State in writing. Audit reports are due within nine months following the end of the audit period.

Further, Section 400(d) requires the State to ensure the subrecipients meet the audit requirements and issue management decisions on audit findings within six months of receiving audit reports and make sure subrecipients take appropriate and timely corrective action.

## **CONDITION**

The Department of Health Services (Health Services) lacks an adequate system to ensure that it promptly receives all audit reports from nonprofit subrecipients required to submit them. It also lacks an adequate system to ensure that it issues management decisions on reported findings. We reviewed Health Services' subrecipient monitoring for fiscal year 2000-01 and found three programs where Health Services did not promptly receive all audit reports from nonprofit subrecipients. Specifically, Health Services' Special Supplemental Nutrition Program for Women, Infants, and Children (WIC Program) did not receive audit reports from 5 of 42 nonprofit subrecipients, and received 8 audit reports from 2 to 143 days late. Similarly, Health Services did not receive audit reports from 2 of 23 nonprofit subrecipients of the HIV Care Formula Grants program and received a program-review report rather than an audit report from another subrecipient. Additionally, for the Maternal and Child Health Services Block Grant to the States program, Health Services did not receive 10 of 25 nonprofit subrecipient audit reports, and received 3 that ranged from 10 to 108 days late. Because Health Services lacked a process to identify nonprofit subrecipients that spent \$300,000 or more in federal awards, it cannot be sure that audits were even required for these subrecipients that did not submit audit reports.

Additionally, at the time of our review, Health Services had not issued the required management decisions within six months of receiving audit reports with findings for the one report with findings concerning the WIC Program in our review, and the one report with findings concerning the HIV Care Formula Grants program in our review.

Without effective systems that identify nonprofit subrecipients required to have audits and track the prompt receipt of these required audit reports, Health Services cannot ensure that its nonprofit subrecipients are meeting audit requirements and are spending program funds according to applicable laws and regulations. Furthermore, when it does not issue management decisions on audit findings affecting its programs, Health Services cannot ensure that its nonprofit subrecipients are taking prompt and appropriate action to address audit findings.

## **RECOMMENDATIONS**

Health Services should establish procedures for identifying nonprofit subrecipients that must have an OMB Circular A-133 audit performed. Additionally, it should ensure it obtains audit reports from nonprofit subrecipients required to submit a report and should promptly issue the required management decisions on audit findings affecting its programs.

## **DEPARTMENT'S VIEW AND CORRECTIVE ACTION PLAN**

Health Services concurs with the finding. Health Services has taken steps to include language in its contracts requiring its subrecipients to submit OMB A-133 audit reports when required and certifications when an OMB A-133 audit is not required.

Additionally, Health Services will ensure that it includes all applicable federal laws, regulations, and the provisions of the grant award in all contracts with its subrecipients. The Maternal and Child Health Branch will continue to work with programs within the Primary Care and Family Health (PCFH) Division through quarterly meetings and will establish written guidelines to coordinate the ongoing subrecipient monitoring process. In addition, the Department of Health Services' WIC Branch and the HIV Care Formula Grants program, as well as other PCFH programs, will develop a joint process to issue management decisions for all audits for its subrecipients with findings. Further, the HIV Care Formula Grants program states that it is setting up a database that will allow it to better track and follow up on late A-133 audit reports. It will then include these steps in applicable procedures manuals.

### **U.S. DEPARTMENT OF AGRICULTURE**

Federal Catalog Number:	10.557
Federal Program Title:	Special Supplemental Nutrition Program for Women, Infants, and Children
Federal Award Numbers and Calendar Years Awarded:	7CA700CA7; 1999 7CA700CA7; 2000

### **U.S. DEPARTMENT OF HEALTH AND HUMAN SERVICES**

Federal Catalog Number:	93.917
Federal Program Title:	HIV Care Formula Grants
Federal Award Numbers and Calendar Years Awarded:	5X07HA00041-10; 2000 2X07HA00041-11; 2001

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Federal Catalog Number:	93.994
Federal Program Title:	Maternal and Child Health Services Block Grant to the States
Federal Award Numbers and Calendar Years Awarded:	6B04MC00336-03; 1999 6B04MC00336-04; 2000

## **U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT**

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Reference Number: 2001-9-7

Federal Catalog Number: 14.239

Federal Program Title: HOME Investment Partnerships Program

Federal Award Numbers and  
Calendar Years Awarded: M 93-SG 060100; 1993  
M 94-SG 060100; 1994  
M 95-SG 060100; 1995  
M 96-SG 060100; 1996  
M 97-SG 060100; 1997  
M 98-SG 060100; 1998  
M 99-SG 060100; 1999  
M 00-SG 060100; 2000

Category of Finding: Suspension and Debarment

State Administering Department: Department of Housing and  
Community Development

### **CRITERIA**

Our review of the HOME Investment Partnerships Program (HOME program) identified the following compliance requirements related to suspension and debarment:

The Code of Federal Regulations, Title 24, Section 24.225, prohibits the State from knowingly doing business with any party that is suspended, debarred, or otherwise ineligible to participate in federal assistance programs. Further, Section 24.510 requires the State to obtain signed certifications from participating organizations regarding debarment, suspension, ineligibility, and involuntary exclusion.

### **CONDITION**

The Department of Housing and Community Development (HCD) does not require subrecipients of HOME program funds to submit suspension and debarment certifications. When HCD does not obtain the required certifications, it risks unknowingly allowing suspended or debarred parties to participate in the federal program. For the transactions we reviewed, we used an alternative test to determine that these subrecipients were not suspended or debarred.

## **RECOMMENDATION**

HCD should establish procedures to ensure that subrecipients submit suspension and debarment certifications before approving their participation in the HOME program.

## **DEPARTMENT'S VIEW AND CORRECTIVE ACTION PLAN**

HCD concurs with the finding. HCD notes that it currently requires subrecipients participating in the HOME program to verify that any contractors receiving HOME funds are not debarred or suspended. HCD enforces this requirement before it releases funds to subrecipients. Further, HCD has verified that all cities, counties and nonprofit housing development organizations (CHDOs) receiving HOME funds have not been debarred or suspended.

HCD states that it will now require at the time of application that all cities, counties and CHDOs certify that they are not suspended or debarred from receiving federal funds. Also, the existing language in the standard agreement requiring HOME subrecipients to certify compliance with the federal regulation will be amended to reflect that the subrecipient is not suspended or debarred.

**U.S. DEPARTMENT OF LABOR  
U.S. DEPARTMENT OF EDUCATION**

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Reference Number: 2001-2-1

Category of Finding: Allowable Costs and Cost Principles

State Administering Department: Employment Development Department

(See listing of the specific federal program details following the discussion of the issues below.)

**CRITERIA**

Our review of federal programs at the Employment Development Department (EDD) determined that the following are among the compliance requirements for allowable costs and cost principles:

The U.S. Office of Management and Budget Circular A-87, *Cost Principles for State, Local and Indian Tribal Governments*, Attachment A, Section C(1)(b), states for costs to be allowable under federal awards, they must be allocable to federal awards under the provisions of the circular. Also, Attachment A, Section C(3)(a), states that a cost is allocable to a particular cost objective (that is, a grant) if the goods or services involved are chargeable or can be assigned to said cost objective in accordance with the relative benefits received. Finally, Attachment B, Section 11.h(5)(e), states that budget estimates or other distribution percentages determined before the services are performed do not qualify as support for personal service charges to a federal grant but may be used in the interim if the system for establishing the estimates produces reasonable approximations of the activity actually performed. Further, at least quarterly, these estimated costs should be compared with actual costs reflecting actual activity.

**CONDITION**

EDD lacked documentation supporting the basis of its allocation for some of its payroll and operating costs charged to federal programs. For 7 of the 30 payroll transactions we reviewed, EDD allocated the payroll costs to federal programs based on estimates of the time staff spent administering the various federal programs instead of using actual time worked. EDD also allocated 5 of 10 operating costs we reviewed among various federal programs that were based on similar estimates. Although EDD indicated that it based the percentages it used to allocate the payroll and operating costs on a workload analysis, it could not provide us with this analysis.

Furthermore, EDD could not demonstrate that it revised the percentages quarterly to reflect more current circumstances, nor could it show it adjusted charges to federal programs to reflect actual activity. As a result of EDD's inability to support the basis of



its allocations, we could not determine whether EDD appropriately allocated 7 payroll transactions and 5 operating costs totaling approximately \$125,000 among various state and federal programs. We were unable to determine the full impact of this issue because EDD was unable to provide us with the total amount it allocated using estimates for fiscal year 2000-01.

We reported a similar finding in our audit for fiscal years 1998-99 and 1999-2000. According to EDD, it has since reviewed the allocation codes and is working toward eliminating unnecessary codes. Furthermore, it has developed and disbursed general guidelines for staff to follow when establishing and documenting allocation codes. EDD plans to fully implement the guidelines and develop documentation for all allocation codes during fiscal year 2001-02.

## **RECOMMENDATION**

To ensure that charges to federal programs are appropriate, EDD should develop an allocation process that bases charges on actual hours worked. When EDD allocates costs using estimates, it should ensure that the bases of the estimates are supported by the appropriate analyses, that the estimates are revised at least quarterly to reflect necessary changes, and that the costs charged to the federal awards are adjusted to reflect the actual activity performed.

## **DEPARTMENT'S VIEW AND CORRECTIVE ACTION PLAN**

EDD concurs with the finding and states that, as of July 1, 2001, it has implemented a new allocation code process. According to EDD, the new process established guidelines that should satisfy federal requirements. In addition, EDD indicates that use of allocation codes is more restrictive and it is requiring staff to justify, document, and perform annual reviews of the allocation codes it continues to use.

### **U.S. DEPARTMENT OF LABOR**

Federal Catalog Number:	17.207
Federal Program Title:	Employment Service
Federal Award Number and Calendar Year Awarded:	ES-10662-00-55; 2000

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Federal Catalog Number:	17.225
Federal Program Title:	Unemployment Insurance
Federal Award Number and Calendar Year Awarded:	UI-10924-00-55; 2000

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Federal Catalog Number: 17.255  
Federal Program Title: Workforce Investment Act  
Federal Award Number and  
Calendar Year Awarded: AA-10295-00-50; 2000

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Federal Catalog Number: 17.801  
Federal Program Title: Disabled Veterans' Outreach Program  
Federal Award Number and  
Calendar Year Awarded: E-9-5-1-5085; 2000

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Federal Catalog Number: 17.804  
Federal Program Title: Local Veterans' Employment  
Representative Program  
Federal Award Number and  
Calendar Year Awarded: E-9-5-1-5085; 2000

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Federal Catalog Number: 17.253  
Federal Program Title: Welfare-to-Work Grants to  
States and Localities  
Federal Award Numbers and  
Calendar Years Awarded: Y-6566-8-00-81-50; 1998;  
Y-7432-9-00-81-50; 1999

#### **U.S. DEPARTMENT OF EDUCATION**

Federal Catalog Number: 84.278  
Federal Program Title: School-to-Work State  
Implementation Grants  
Federal Award Number and  
Calendar Year Awarded: V278E70020; 2000

## **U.S. DEPARTMENT OF TRANSPORTATION**

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Reference Number:	2001-9-1
Federal Catalog Number:	20.205
Federal Program Title:	Highway Planning and Construction
Federal Award Number and Calendar Year Awarded:	N 4520.162; 2000
Category of Finding:	Procurement, Suspension and Debarment, Special Tests and Provisions
State Administering Department:	Department of Transportation

### **CRITERIA**

Our review of the Highway Planning and Construction program identified the following compliance requirement:

The Code of Federal Regulations, Title 49, Section 18.42, in part, requires the State to retain all financial and programmatic records, supporting documents, statistical records, and other records and documents considered as pertinent to program regulations or the grant agreement for a three year period starting on the day the grantee, which is the State, submits its final expenditure report to the U.S. Department of Transportation, Federal Highway Administration (FHWA).

### **CONDITION**

The California Department of Transportation (Caltrans) could not always locate its contract files or other documents needed to show that it complied with certain federal requirements for its highway construction projects. More specifically, of 40 contracts we selected to test, Caltrans could not locate the contract file for 5 contracts, and the contract files for another 12 were incomplete. The awards for these 17 contracts totaled more than \$1.1 billion. As a result, we could not test whether Caltrans obtained the appropriate FHWA and state approvals for 14 contracts, obtained from contractors the required suspension or debarment certifications for 10 contracts, used the appropriate competitive process for 10 contracts, or obtained FHWA approval of major contract change orders for 9 contracts. Furthermore, for the one major contract change order we were able to test, Caltrans could not locate the document that showed it obtained FHWA's written approval before proceeding with the related construction, although Caltrans indicated it had received verbal approval. This change order increased the amount of the contract by more than \$367,000 and added 22 working days to the contract's length. Finally, we could not ensure that one of

Caltrans' district offices performed quality assurance testing on materials and workmanship it used for 2 of 10 construction projects we tested, because it could not locate the supporting documents. As a result, we cannot conclude that Caltrans fulfilled its responsibilities related to these compliance requirements. In addition, when Caltrans does not properly maintain documents that demonstrate its compliance with federal requirements for its highway construction projects, it runs the risk of incurring costs that FHWA may not reimburse.

## **RECOMMENDATIONS**

Caltrans should improve its system of tracking contract files and other documents for its highway construction projects as well as ensure that the contract files are complete.

## **DEPARTMENT'S VIEW AND CORRECTIVE ACTION PLAN**

Caltrans agrees with the finding and states that staffing issues, a lack of procedures, and inadequate file space caused the condition. According to Caltrans, it has resolved the staffing issue and is working towards obtaining adequate space for the contract files by December 2002. In addition, Caltrans states that it will complete a comprehensive business process review of the filing system and train its staff on the improved procedures resulting from the review by June 2002.

Regarding the lack of written FHWA approval of contract change orders, Caltrans states that it recently clarified the section of its Construction Manual that describes the approval process. Caltrans is also developing a course on contract change orders which is intended to provide instruction on the requirements for FHWA approval. This course will begin in February 2002 and will target Caltrans' Resident Engineers.

Finally, in July 2001, Caltrans began training district field office staff on "Field Office Procedures for Statewide Consistency" to improve controls over its records of testing materials and workmanship.

# FEDERAL EMERGENCY MANAGEMENT AGENCY

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Reference Number: 2001-8-1  
Federal Catalog Number: 83.544  
Federal Program Title: Public Assistance Grants  
Year Awarded: State fiscal year 2000-01  
Category of Finding: Period of Availability  
State Administering Department: Office of Emergency Services

## CRITERIA

Our review of the Public Assistance Grants program determined that the following compliance requirement relates to period of availability:

The Code of Federal Regulations, Title 44, sections 206.204(c) and (d), establishes time limits for completing the various types of work funded through the Public Assistance Grants program.

## CONDITION

The Office of Emergency Services (Emergency Services) cannot ensure that the services it is paying for are within the allowable time period. Emergency Services makes payments to its subrecipients after the subrecipients submit a payment-request document. However, these forms do not include the time period during which the services being reimbursed occurred. Most of the 40 payments we reviewed were requested while the project was in progress, providing some assurance that the related services were rendered during the period of availability. However, 4 payments totaling more than \$950,000 were requested after the approved project completion date. Thus, we had no such assurance. For example, Emergency Services paid one recipient more than \$652,000 in September 2000—even though the latest time extension for the project had expired six months earlier in April 2000. When Emergency Services does not ensure that work being claimed by its subrecipients occurred within approved time frames, it runs the risk of payments being disallowed by the federal government.

## **RECOMMENDATION**

Emergency Services should require its subrecipients to provide sufficient information on their payment requests to allow it to determine if the services being reimbursed were completed within the allowable time periods. If payment requests are for services that were not provided within the approved time periods, Emergency Services should not approve the payment.

## **DEPARTMENT'S VIEW AND CORRECTIVE ACTION PLAN**

Emergency Services (OES) agrees that current payment processes are not sufficient to determine if subrecipient reimbursement requests are for services provided within approved time periods. However, OES disagrees that the auditor's recommendation will reduce the risk of inappropriate payments to subrecipients. Instead, OES has initiated a comprehensive review of its disaster assistance grant management system to identify areas for improvement, including linking grant payment processes with on-going grant monitoring processes. OES anticipates implementing changes to its current grant management system for open and material grants during fiscal year 2002-03.

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Reference Number:	2001-9-5
Category of Finding:	Suspension and Debarment
State Administering Department:	Office of Emergency Services

(See listing of the specific federal program details following the discussion of the issues below.)

## **CRITERIA**

Our review of the Public Assistance Grants and Hazard Mitigation Grant programs determined that the following compliance requirements relate to suspension and debarment:

The Code of Federal Regulations, Title 44, Section 17.225(a), requires the Office of Emergency Services (Emergency Services) to ensure that it does not make sub-awards to any parties who are debarred, suspended, or otherwise excluded from participation in federal assistance programs. Additionally, Section 17.510(b), requires Emergency Services to obtain certifications that affirm participating parties are not presently debarred or suspended.

## **CONDITION**

Emergency Services did not require Public Assistance Grants and Hazard Mitigation Grant program applicants to submit suspension and debarment certifications. When it does not require these certifications, Emergency Services runs the risk of allowing suspended or debarred parties to participate in the federal programs.

Emergency Services' position is that although it recognizes that federal regulations prohibit it from making sub-awards to suspended, debarred, or otherwise ineligible parties, it believes another federal regulation excludes all transactions for the Public Assistance Grants and Hazard Mitigation Grant programs from the requirement to submit suspension and debarment certifications. This regulation, the Code of Federal Regulations, Title 44, Section 17.110(a)(2)(v), states that one of the exceptions for coverage under the suspension and debarment regulations is "transactions pursuant to national or agency-recognized emergencies or disasters." During our fiscal year 1999-2000 review of these federal programs, we contacted the Federal Emergency Management Agency's (FEMA) legal staff for an interpretation of how this regulation applies. The legal staff indicated that suspension and debarment requirements do not apply to the initial response to a disaster, but would apply to the later recovery transactions.

## **RECOMMENDATIONS**

Emergency Services should obtain written clarification from FEMA as to whether it must obtain suspension and debarment certifications from its subrecipients for the Public Assistance Grants and Hazard Mitigation Grant programs. If FEMA requires it to obtain these certifications, Emergency Services should ensure that it does so before it approves applications for federal program funds.

## **DEPARTMENT'S VIEW AND CORRECTIVE ACTION PLAN**

Emergency Services disagrees with this finding and with the verbal interpretation given by FEMA counsel. Emergency Services' position is that Public Assistance and Hazard Mitigation subrecipients are exempt from the requirement to submit the suspension and debarment certification identified in the Code of Federal Regulations, Title 44, Section 17.

FEMA's Office of Inspector General recently completed an audit of Emergency Services' management of the Public Assistance and Hazard Mitigation programs. The audit scope included a review of both program and financial-related activities for 18 disasters declared from 1983 through 1999. The draft report, issued in August 2001, made no mention of any deficiency in this area, therefore, no further clarification is needed from FEMA.

Emergency Services agrees that subrecipients, in accordance with the Code of Federal Regulations, Title 44, Section 13.35, should not enter into agreements with any parties who are debarred, suspended, or otherwise excluded from participation in federal assistance programs. Current subrecipient monitoring processes include periodic reviews for compliance with Section 13.35. Emergency Services is in the process of developing a Grant Management system which will establish a more routine review to ensure that subrecipients have complied with applicable grant laws and regulations.

### **FEDERAL EMERGENCY MANAGEMENT AGENCY**

Federal Catalog Number: 83.544  
Federal Program Title: Public Assistance Grants  
Year Awarded: State fiscal year 2000-01

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Federal Catalog Number: 83.548  
Federal Program Title: Hazard Mitigation Grant  
Year Awarded: State fiscal year 2000-01

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Reference Number: 2001-12-4  
Category of Finding: Reporting  
State Administering Department: Office of Emergency Services

(See listing of the specific federal program details following the discussion of the issues below.)

### **CRITERIA**

Our review of the Public Assistance Grants and Hazard Mitigation Grant programs determined that the following compliance requirements relate to reporting:

The Code of Federal Regulations, Title 44, Section 13.20, requires the State to maintain accounting records to properly track and accurately report financial activities related to federal grants. Additionally, Section 13.41(b), requires the State to use the financial status report form to report the status of funds for all nonconstruction grants. To meet this requirement for both the Public Assistance Grants and Hazard Mitigation Grant programs, the Federal Emergency Management Agency (FEMA) requires the



Office of Emergency Services (Emergency Services) to submit quarterly financial status reports for each disaster. FEMA mandates that the status reports are to include total federal expenditures, including administrative allowances, and total recipient expenditures, excluding amounts for administration.

## **CONDITION**

Emergency Services' financial status reports contain unsupported expenditure information. As a result, FEMA cannot rely on these reports to accurately assess program status. Rather than basing its and the subrecipients' share of expenditures on information from its accounting records, Emergency Services inappropriately uses a formula to derive this amount. Emergency Services uses this formula because it does not completely track expenditure information from subrecipients. Emergency Services' use of formulas can also result in errors. For example, in one report we tested, Emergency Services inappropriately included \$36,722 in administrative costs in its reported recipient expenditures. To report recipient expenditures, Emergency Services uses its federal expenditures to derive its state and local expenditure amounts. However, although federal guidelines require Emergency Services to include administrative costs when reporting federal expenditures, it should exclude administrative costs when reporting state and local expenditures.

Additionally, Emergency Services does not separately account for the amount of state funds it expends administering these two federal programs. As a result, even if it did use its accounting records for reporting expenditure information, Emergency Services could not assure the accuracy of the amount of administrative expenditures that it reported to the federal government.

## **RECOMMENDATIONS**

Emergency Services should ensure that its accounting records support its financial status reports. Additionally, it should separately account for and report on state administrative costs expended on federal disasters and subrecipient expenditures.

## **DEPARTMENT'S VIEW AND CORRECTIVE ACTION PLAN**

Before January 1999, FEMA required financial status reports to be filed upon closure of disasters, after final inspection and financial reconciliation of all subgrantee records. FEMA notified Emergency Services in January 1999 that financial status reports would be required on a quarterly basis for all disasters. Emergency Services has made several attempts to discuss with FEMA how best to report California disaster activity, which currently involve more than 35,000 individual projects, into a single, generic federal report format. In addition, Emergency Services has requested guidance on how to report the timing differences between expenditures and fund disbursements that are associated with federal regulatory requirements placed on the State. For example, in any given disaster as much as 30 percent of the disaster funds

can be associated with small projects. In accordance with federal regulations, disaster funds for small projects are advanced to subgrantees at the time of approval; thus, disbursement occurs prior to any actual expenditures being incurred. Consequently, a quarterly report of on-going disaster activity will have some portion of federal disbursements without associated expenditures. Emergency Services will continue to seek an active dialogue with FEMA to reach consensus on how to report on-going disaster assistance activity without creating a burdensome workload.

### **FEDERAL EMERGENCY MANAGEMENT AGENCY**

Federal Catalog Number: 83.544  
Federal Program Title: Public Assistance Grants  
Year Awarded: State fiscal year 2000-01

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Federal Catalog Number: 83.548  
Federal Program Title: Hazard Mitigation Grant  
Year Awarded: State fiscal year 2000-01

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Reference Number: 2001-12-5  
Category of Finding: Reporting  
State Administering Department: Office of Emergency Services

(See listing of the specific federal program details following the discussion of the issues below.)

### **CRITERIA**

Our review of the Public Assistance Grants and Hazard Mitigation Grant programs determined that the following compliance requirement relates to reporting:

The Code of Federal Regulations, Title 44, Section 13.20, requires the State to maintain accounting records to properly track and accurately report financial activities related to federal grants.

## **CONDITION**

In fiscal year 2000-01, the Office of Emergency Services (Emergency Services) did not reconcile the receipts and disbursements reported in its federal cash transaction reports to its official accounting records. As a result, we could not determine whether the receipts and disbursements reported in the quarterly federal cash transaction reports agreed with Emergency Services' accounting records.

## **RECOMMENDATION**

Emergency Services should reconcile the receipts and disbursements reported in its federal cash transaction reports to the receipts and disbursements recorded in its accounting records.

## **DEPARTMENT'S VIEW AND CORRECTIVE ACTION PLAN**

Increased workloads and the inability to obtain additional positions to hire qualified staff with the level of expertise to perform these functions have been a mitigating factor currently and in the past. Emergency Services plans to continuing pursuing requests for additional staffing in order to comply with the recommendation.

### **FEDERAL EMERGENCY MANAGEMENT AGENCY**

Federal Catalog Number:	83.544
Federal Program Title:	Public Assistance Grants
Year Awarded:	State fiscal year 2000-01

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Federal Catalog Number:	83.548
Federal Program Title:	Hazard Mitigation Grant
Year Awarded:	State fiscal year 2000-01

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Reference Number:	2001-13-3
Category of Finding:	Subrecipient Monitoring
State Administering Department:	Office of Emergency Services

(See listing of the specific federal program details following the discussion of the issues below.)

## **CRITERIA**

Our review of the Public Assistance Grants and Hazard Mitigation Grant programs determined that the following compliance requirements relate to subrecipient monitoring:

The U.S. Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations* (OMB Circular A-133), requires subrecipients spending more than \$300,000 in federal assistance to submit audit reports to the State within nine months of the end of their fiscal year. If an audit finds that a subrecipient has failed to comply with federal program requirements, OMB Circular A-133 also requires the State to issue a management decision regarding the resolution of the audit finding within six months of receiving the audit report and ensure that the subrecipient proceeds with corrective action as rapidly as possible.

## **CONDITION**

During fiscal year 2000-01, the Office of Emergency Services (Emergency Services) did not have a system in place to ensure that its nonprofit subrecipients spending more than \$300,000 in federal funds submitted required audit reports. Emergency Services said it previously contracted with the State Controller's Office to fulfill these responsibilities. However, Emergency Services did not renew its contract with the State Controller's Office for these services for audits of fiscal years after 1998-99, and it has since failed to complete these responsibilities itself. As a result, Emergency Services has no assurance that its nonprofit subrecipients spending more than \$300,000 complied with applicable federal requirements. During fiscal year 1999-2000 (for which applicable audit reports would have been due to the State during fiscal year 2000-01), Emergency Services paid more than \$1.4 billion in federal funds to 27 nonprofit subrecipients.

Additionally, for the audit reports of its local government subrecipients, Emergency Services did not ensure that a management decision regarding the resolution of audit findings was made within six months after it received an audit report. During fiscal year 2000-01, the State Controller's Office reviewed the annual audit reports of local governmental agencies receiving more than \$300,000 and forwarded three reports containing seven findings to Emergency Services for resolution. According to Emergency Services, it did not receive two of the reports, which represent four of the seven findings and, therefore, did not take any action to resolve the findings. For the remaining report, representing three findings, Emergency Services stated it had followed up and resolved the subrecipient's audit findings. However, it did not issue written management decisions that clearly state whether the audit findings were sustained, the reasons for its decisions, and the actions it expected the auditee to take to resolve the audit findings.

## **RECOMMENDATIONS**

Emergency Services should establish controls to ensure that private, nonprofit subrecipients receiving more than \$300,000 in federal grant funds are audited annually. Additionally, Emergency Services should promptly follow up on all reported audit findings concerning subrecipients, and ensure that written management decisions regarding the resolution of audit findings are issued within six months of its receipt of the subrecipients' audit report.

## **DEPARTMENT'S VIEW AND CORRECTIVE ACTION PLAN**

Emergency Services agrees with the recommendation and has taken corrective action. In November 2000, Emergency Services formed a new unit whose responsibilities include ensuring that subrecipients meet the audit requirements of OMB Circular A-133. Additionally, this unit will promptly follow up on all reported audit findings concerning subrecipients, and ensure that written management decisions regarding the resolution of audit findings are issued within six months of its receipt of the subrecipients' audit report.

### **FEDERAL EMERGENCY MANAGEMENT AGENCY**

Federal Catalog Number:	83.544
Federal Program Title:	Public Assistance Grants
Year Awarded:	State fiscal year 2000-01

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Federal Catalog Number:	83.548
Federal Program Title:	Hazard Mitigation Grant
Year Awarded:	State fiscal year 2000-01

## U.S. DEPARTMENT OF EDUCATION

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Reference Number: 2001-2-3

Federal Catalog Number: 84.011

Federal Program Title: Migrant Education—Basic State Grant Program

Federal Award Number and Calendar Year Awarded: S011A000005; 2000

Category of Finding: Allowable Costs and Cost Principles

State Administering Department: Department of Education

### CRITERIA

Our review of the Migrant Education—Basic State Grant Program (Migrant Education) identified the following compliance requirement related to allowable costs and cost principles:

The U.S. Office of Management and Budget Circular A-87, *Cost Principles for State, Local and Indian Tribal Governments* (OMB Circular A-87), Attachment A, Section (C), states that for costs to be allowable under a federal award, costs must be necessary and reasonable for the proper and efficient performance and administration of federal awards.

### CONDITION

The Department of Education (Education) did not always determine the cost-effectiveness of the State's use of Migrant Education funds. Education paid one subrecipient more than \$29,000 in overhead costs to administer a contract that Education should more appropriately administer. Specifically, Education allocates Migrant Education funds to 22 migrant education regional offices statewide. In addition, because the U.S. Department of Education requires Education to report the number of migrant children in California eligible for the program, the 22 regional offices enter data regarding eligible migrant children into a computer system.

The data are transmitted to a vendor who combines the data from all the regional offices, ensures that migrant children are not counted more than once, and calculates the number of eligible migrant children in California. Although Education administers the contract with this vendor, Education pays one regional office to administer a contract with another vendor that provides software and technical assistance to the statewide regional offices for the development and entry of their

count data. The vendor services appear to be an appropriate use of Migrant Education funds. However, Education should more appropriately administer this contract because it is for assistance to the regional offices statewide, and not just for the one regional office. As a result, the additional \$29,000 in overhead costs that Education paid the one region for its administration of the contract may not be necessary for the proper and efficient performance and administration of the program. According to Education, it is seeking to enter into a sole-source contract with the vendor and is nearing the final stages of the process at which point it will begin administering the contract. However, during fiscal year 2000-01, the regional office continued to administer the contract.

Education also approved the use of \$85,850 in Migrant Education funds without determining whether the use was reasonable as required by OMB Circular A-87. Education used the funds to pay for vehicle leases, insurance, and maintenance in two regional offices and for a vehicle purchase in a third regional office. However, Education did not follow its own policy, which requires it to approve vehicle leases or purchases only if program subrecipients can show it is more cost-effective to lease or purchase vehicles than to reimburse individuals who drive their personal vehicles on Migrant Education business. When Education approves the use of Migrant Education funds without assessing the cost-effectiveness of the regional offices' proposed use of these funds, it cannot assure the efficient and effective use of federal program funds.

## **RECOMMENDATIONS**

Education should continue its efforts to take on the contract administration responsibilities for the software and technical assistance contract. In addition, Education should ensure that it approves only allowable costs that are reasonable and necessary to perform the program. It should also follow its program policy for the approval of vehicle leases or purchases.

## **DEPARTMENT'S VIEW AND CORRECTIVE ACTION PLAN**

**Administration of the Contract:** The region that temporarily contracted with the Tromik Technology Corporation (for services to the 22 migrant education regions) had some overhead costs for administering this contract. Tromik continues to provide technical assistance to the 22 migrant education regions. Migrant Education is currently in the process of obtaining the services of Tromik through a sole-source contract. The proposed sole-source contract period is January 1, 2002, through December 31, 2002.

**Leases:** As a result of the fiscal year 2000-2001 findings, Migrant Education has developed a Cost Analysis Worksheet for migrant education regions. Regions use this form (or may use their own format) to show the reasonableness of costs associated with leases and/or purchases of vehicles. A region will show that it is more cost effective to lease or purchase vehicles rather than to reimburse individuals on a

daily basis prior to entering into a future lease/purchase contract. The submittal of this information was required with their regional applications for fiscal year 2001-2002. If the analysis showed that it is not cost effective, Migrant Education informed the region to terminate the lease/purchase contract as soon as legally feasible. The regions will maintain a complete analysis worksheet on file for all vehicle lease/purchase contracts approved by Education/Migrant Education.

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Reference Number:	2001-3-2
Federal Catalog Number:	84.181
Federal Program Title:	Special Education—Grants for Infants and Families with Disabilities
Federal Award Number and Calendar Year Awarded:	H181A000037; 2000
Category of Finding:	Cash Management
State Administering Department:	Department of Developmental Services

## **CRITERIA**

Our review of the Special Education—Grants for Infants and Families with Disabilities program (Early Intervention) identified the following compliance requirements relating to cash management:

The Code of Federal Regulations, Title 31, Part 205, Subpart B, provides the cash management requirements for programs not covered in the Cash Management Improvement Act agreement between the U.S. Department of the Treasury and the State. Section 205.20 of this subpart requires the State to limit the cash advances from the U.S. Department of the Treasury to the minimum amounts needed and to time the advances, as close as it can, with the actual and immediate cash needs of the State to carry out the program.

## **CONDITION**

The Department of Developmental Services (Developmental Services) did not always minimize the amount of time elapsing between the transfer of Early Intervention federal funds to the State and their disbursement for program costs. Specifically, the time between the receipt of federal funds and the issuance of warrants in 29 of 36 transactions ranged from 5 to 58 days. For 12 of those transactions, the elapsed time was 10 days or more. When Developmental Services



does not minimize the amount of time between the receipt and disbursement of federal funds, the State improperly earns interest while federal funds are held in State accounts. For the 29 transactions, we estimate that the State earned about \$16,500 in interest.

## **RECOMMENDATION**

To minimize the time elapsing between the receipt and disbursement of federal funds, Developmental Services should request federal funds closer to the date warrants for program costs are released.

## **DEPARTMENT'S VIEW AND CORRECTIVE ACTION PLAN**

Developmental Services acknowledges that the time between receipt and disbursement of federal funds was not always minimized. Further, it states that it has current procedures to minimize the risk of having federal funds in hand for too long a period before disbursements are made. However, Developmental Services notes that despite stamping payment requests as "federal fund expenditures," a possible cause for the delays may be its no longer using special expedite tags for the requests. Developmental Services states that it will discuss this problem with the State Controller's Office to determine what steps can be taken to assure that these types of payment delays do not occur in the future and will implement additional cash monitoring procedures for any federal funds.

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Reference Number:	2001-3-3
Category of Finding:	Cash Management
State Administering Department:	Department of Education

(See listing of the specific federal program details following the discussion of the issues below.)

## **CRITERIA**

Our review of federal programs identified the following requirements relating to cash management:

The Code of Federal Regulations, Title 34, Section 80.21, allows a state's subrecipients to receive advance payments provided they demonstrate the ability to minimize the time elapsing between the receipt and disbursement of federal funds. Otherwise, reimbursement is the preferred method of payment. Further, this section requires a state's subrecipients to promptly pay to the federal agency any interest greater than \$100 that they earned on the advances. Additionally, if a

state's subrecipients receive advance payments, Section 80.20(b)(7) requires them to follow procedures for minimizing the time between the receipt and disbursement of federal funds.

## **CONDITION**

The Department of Education (Education) does not have adequate procedures to ensure that program subrecipients minimize the time elapsing between their receipt and use of federal program funds. Under its payment procedures, Education disburses predetermined percentages of program funds to subrecipients rather than assessing and disbursing funds based on each subrecipient's immediate cash needs. Further, Education does not always require subrecipients to report on their use of program advances before making additional payments to the subrecipients. Combining Education's inadequate procedures to assess each subrecipient's cash needs with its predetermined advance-payment process does not ensure that subrecipients minimize the time elapsing between their receipt and disbursement of federal program funds.

Of the 40 expenditure transactions we reviewed for the Migrant Education—Basic State Grant Program, 37 were payments to 18 of Education's 22 regional offices. We compared Education's first advance payment to these regional offices against their mid-year expenditure reports, and found that 6 had high ending cash balances ranging from \$80,300 to \$964,900. We considered any positive balance high because Education disbursed the first advance payment, approximately 40 percent of the sub-awards, by November 2000. This was at least three months before the end of the six-month period for which the regional offices reported expenditures. Further, for 1 of these 18 regional offices, Education did not receive a six-month expenditure report; therefore, it could not determine this region's cash balance.

Additionally, for the Special Education—Grants for Infants and Families with Disabilities program, 9 of the 40 subrecipients we reviewed received higher cash advances than needed that ranged from \$4,500 to \$36,600. Education paid these 9 subrecipients approximately 50 percent of their sub-awards in April 2001, but did not assess their cash needs because Education did not receive reports of subrecipient program expenditures as of March 31, 2001, until after it made this first payment. Furthermore, in May 2001, Education paid 7 of these 9 subrecipients an additional 25 percent of their sub-awards. However, before making this payment, Education had received the expenditure reports for 5 of the 7 that showed they did not yet require additional funds. For the remaining 2 subrecipients, Education did not receive the expenditure reports in time to assess their cash needs before it made the second payment.

Finally, for the Class Size Reduction program, Education's first payment to subrecipients was disbursed in February 2001, and was for 80 percent of their sub-awards. However, Education did not assess the subrecipients' cash needs because it did not require them to submit expenditure reports until June 1, 2001. We compared Education's payments to 40 program subrecipients against their expenditure reports and found that 8 out of 26 had ending cash balances that exceeded 10 percent of

their first payment for the current year plus any unspent cash balances carried forward from the previous year. These cash balances ranged from \$700 to \$371,900. For the other 14 subrecipients, Education could not determine their cash balances because 13 had not submitted expenditure reports by June 1, 2001, and 1 submitted an incorrect report.

When Education does not assess its subrecipients' immediate cash needs before making federal program advances, it cannot assure that subrecipients minimize the time elapsing between the receipt and use of federal funds.

Additionally, Education did not require subrecipients to report and remit interest in excess of \$100 earned on these federal program advances. As a result, these subrecipients may use the interest earned on federal program advances for activities that may not be allowable.

## **RECOMMENDATIONS**

To minimize the time elapsing between the receipt and use of federal program funds, Education should implement procedures to assess each subrecipient's cash needs and adjust its advance payments to more closely reflect each of its subrecipients' immediate cash needs. Additionally, Education should ensure its subrecipients report their program expenditures in time to allow Education to assess their cash needs before making additional advance payments. Education should also require subrecipients to report and pay interest earnings greater than \$100 on these advances so it can repay these interest earnings to the federal awarding agency. Finally, if Education cannot demonstrate its ability to ensure subrecipients minimize the time elapsing between the receipt and disbursement of federal program advances, it should implement procedures to pay its subrecipients on a reimbursement basis rather than paying them in advance.

## **DEPARTMENT'S VIEW AND CORRECTIVE ACTION PLAN**

The Local Education Agencies (LEAs) receive an initial advance based on their grant award. Migrant Education, Special Education and Class Size Reduction will require each LEA to submit an interim expenditure report before the next apportionment is made. Based on information reported in the expenditure report, Migrant Education, Special Education and Class Size Reduction may make adjustments to the LEAs' next apportionment.

Migrant Education, Special Education and Class Size Reduction have added an additional reporting field to the expenditure report requesting the amount of interest earned over \$100. Education will explore options in determining the best approach to take in recovering any interest earned over \$100.

## U.S. DEPARTMENT OF EDUCATION

Federal Catalog Number: 84.011  
Federal Program Title: Migrant Education—Basic State  
Grant Program  
Federal Award Number and  
Calendar Year Awarded: S011A000005; 2000

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Federal Catalog Number: 84.181  
Federal Program Title: Special Education—Grants for Infants and  
Families with Disabilities  
Federal Award Number and  
Calendar Year Awarded: H181A000037; 2000

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Federal Catalog Number: 84.340  
Federal Program Title: Class Size Reduction  
Federal Award Number and  
Calendar Year Awarded: S340A000005A; 2000

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Reference Number: 2001-3-5  
Federal Catalog Number: 84.126  
Federal Program Title: Rehabilitation Services—Vocational  
Rehabilitation Grants to States  
Federal Award Numbers and  
Calendar Years Awarded: H126A000005; 1999  
H126A010005; 2000  
Category of Finding: Cash Management  
State Administering Department: Department of Rehabilitation

## **CRITERIA**

We determined that the following requirements relate to compliance with the Cash Management Improvement Act Agreement (CMIA agreement) between the U.S. Department of the Treasury and the State:

The CMIA agreement, sections 9.4.1 and 9.6.1, establishes requirements for calculating the State's interest liability. Sections 9.4.3 and 9.6.2 provide the methods for calculating this interest liability.

## **CONDITION**

The Department of Finance (Finance) requires state departments to report information related to the receipt and disbursement of federal funds so that it can calculate the State's interest liability under the CMIA agreement. However, our review of the worksheets used in the calculation of the interest liability revealed an error in a formula in the first-quarter worksheet sent to Finance by the Department of Rehabilitation (Rehabilitation). Specifically, the formula that Rehabilitation used to calculate the subtotals for the expenditures did not include two expenditures totaling \$2.5 million. Because of these errors, Finance understated the net federal liability by more than \$110,000 in its CMIA annual report to the federal government. Consequently, the State will not recoup this loss of more than \$110,000 for fiscal year 2000-01 from the federal government until March 2003.

## **RECOMMENDATION**

Rehabilitation should ensure that the quarterly worksheets submitted to Finance are mathematically accurate and complete.

## **DEPARTMENT'S VIEW AND CORRECTIVE ACTION PLAN**

Rehabilitation agrees with the finding and states that it will review its worksheets more closely to prevent this type of error from happening in the future.

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Reference Number:	2001-3-7
Federal Catalog Number:	84.186
Federal Program Title:	Safe and Drug-Free Schools and Communities—State Grants
Federal Award Number and Calendar Year Awarded:	S186B000005; 2000

Category of Finding: Cash Management  
State Administering Department: Department of Alcohol and Drug Programs

## **CRITERIA**

Our review of the Safe and Drug-Free Schools and Communities—State Grants (Safe and Drug-Free Schools) program identified the following compliance requirements relating to cash management:

The Code of Federal Regulations, Title 34, Section 80.21, allows subrecipients to receive advance payments provided they demonstrate the ability to minimize the time elapsing between the receipt and disbursement of federal funds. Otherwise, reimbursement is the preferred method of payment. Further, this section requires subrecipients to promptly pay the federal agency any interest greater than \$100 that they earned on the advances. Additionally, if subrecipients receive advance payments, Section 80.20(b)(7) requires them to follow procedures for minimizing the time between the receipt and disbursement of federal funds.

## **CONDITION**

The Department of Alcohol and Drug Programs (DADP) lacks adequate procedures to ensure that subrecipients of the Safe and Drug-Free Schools program minimize the time elapsing between receipt and use of program funds.

DADP awards subgrants to counties to carry out the program's activities. In accordance with state law, DADP makes monthly subgrant payments to counties regardless of their actual expenditures. DADP also does not require the counties to submit invoices to support the monthly payments. Although DADP is instituting procedures to track county expenditures quarterly to better assess each county's cash needs, it had not yet fully implemented these procedures during fiscal year 2000-01. DADP's target date for full implementation is July 1, 2002. As a result, DADP cannot be sure that counties minimized the time between the counties' receipt and use of federal funds throughout the year.

Additionally, although DADP's agreements with the counties require them to remit interest in excess of \$100 earned on federal program advances, DADP did not require counties to report that interest. As a result, DADP does not know if any counties earned interest greater than \$100 on federal program advances and whether counties should be remitting interest earnings to it.

## **RECOMMENDATIONS**

DADP should continue implementing its new procedures to ensure that the counties participating in the program minimize the time elapsing between their receipt and use

of federal program funds. DADP should also require the counties to report and pay DADP any interest earnings greater than \$100 on these advances so it can repay these interest earnings to the federal awarding agency.

## **DEPARTMENT'S VIEW AND CORRECTIVE ACTION PLAN**

DADP will continue to implement procedures to ensure that counties minimize the time elapsing between receipt and use of federal program funds.

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Reference Number:	2001-3-8
Category of Finding:	Cash Management
State Administering Department:	California Community Colleges, Chancellor's Office

(See listing of the specific federal program details following the discussion of the issues below.)

## **CRITERIA**

Our review of federal programs identified the following requirements relating to cash management:

The Code of Federal Regulations, Title 34, Section 80.21, allows subrecipients to receive advance payments provided they demonstrate the ability to minimize the time elapsing between the receipt and disbursement of federal funds. Otherwise, reimbursement is the preferred method of payment. Further, except in certain circumstances, this section requires subrecipients to promptly pay to the federal agency any interest greater than \$100 per year that they earned on the advances. Additionally, if subrecipients receive advance payments, Section 80.20(b)(7) requires them to follow procedures for minimizing the time between the receipt and disbursement of federal funds.

## **CONDITION**

The California Community Colleges, Chancellor's Office (Chancellor's Office) does not have adequate procedures to ensure that subrecipients of the Vocational Education—Basic Grants to States program (Vocational Education) and the Tech-Prep Education program (Tech-Prep) minimize the time elapsing between their receipt and use of federal program funds. Under its payment procedures, the Chancellor's Office approves program advances for each subrecipient and disburses these advances monthly based on predetermined percentages. However, because the

Chancellor's Office approves advances that exceed some subrecipients' immediate cash needs, some subrecipients carry excessive cash balances during the fiscal year. Further, the Chancellor's Office does not require subrecipients to report and pay it the excess interest earned on these federal program advances.

The Chancellor's Office approves subrecipient applications, calculates advances equal to 84 percent of the subrecipients' approved allocations, and pays these advances in monthly installments. However, because these advances are not based on each subrecipient's cash needs, some subrecipients receive monthly advance payments that may exceed their immediate cash needs. To determine if a subrecipient's spending appears reasonable, the Chancellor's Office uses the subrecipients' quarterly year-to-date expenditures and progress reports to compare the reported expenditures to the amounts it advanced to each subrecipient. If it determines that a subrecipient's spending appears reasonable, the Chancellor's Office authorizes further advance payments; otherwise, it may contact the subrecipient to obtain an explanation of expenses, reduce the subrecipient's monthly advance payments, or deny additional payments. However, the Chancellor's Office does not specify or provide guidance on what level of spending it considers reasonable. Furthermore, when the Chancellor's Office determines that a reduction in the monthly advance payment amount is warranted, it begins making these adjustments in the third quarter of the fiscal year.

Our review of the Chancellor's Office payments to subrecipients of the Vocational Education program and the subrecipients' reported expenditures found that 17 of the 25 subrecipients we reviewed maintained high cash balances ranging from \$14,138 to \$566,319 for one or more quarters. We considered balances high when they exceeded 10 percent of the amounts advanced by the Chancellor's Office. Similarly, for the Tech-Prep program, 9 of the 13 subrecipients we reviewed maintained high cash balances ranging from \$7,326 to \$112,942 for one or more quarters. Because the Tech-Prep program subgrants are small, we considered balances high when they exceeded \$7,000 and 10 percent of the amounts advanced for this program.

The Chancellor's Office stated that because some subrecipients experience delays in posting expenditures to their accounting records, these subrecipients underreport the program funds spent during the interim quarters. The Chancellor's Office asserts that most subrecipients spend all the program funds they receive by the last quarter. However, the Chancellor's Office is responsible for ensuring that subrecipients minimize the time between the subrecipients' receipt and use of federal funds throughout the year. When the Chancellor's Office does not adequately assess its subrecipients' immediate cash needs before approving monthly advances, it cannot assure that subrecipients minimize the time elapsing between the receipt and use of federal funds.

Additionally, the Chancellor's Office did not require subrecipients to report and pay it interest exceeding \$100 earned on these federal program advances. As a result, these subrecipients may use the interest earned on federal program advances for activities that may not be allowable.



## **RECOMMENDATIONS**

To minimize the time elapsing between the receipt and use of federal program funds, the Chancellor's Office should use relevant spending data to assess each of its subrecipients' immediate cash needs and approve initial advances that reflect these needs. Additionally, the Chancellor's Office should ensure its subrecipients promptly post their expenditure transactions so that their expenditure reports reflect the most current actual program expenditures. The Chancellor's Office should also require subrecipients to report and pay interest earnings greater than \$100 on these advances so it can repay these interest earnings to the federal awarding agency.

## **DEPARTMENT'S VIEW AND CORRECTIVE ACTION PLAN**

The 2001-02 Vocational and Technical Education (VTEA) Title IC funds were certified for apportionment based upon each district's expenditures through the third quarter of 2000-01. Districts were certified at either 66% or 83% of their tentative allocations (districts receive 84% of the amount certified). The 2001-02 VTEA Title IB funds and Title II funds were certified at 100% of their grant amount (districts receive 84% of the amount certified). The rationale for this is that the Title IB grants were funded from March 2001 through June 2002, and the potential of a low rate of expenditures in the first quarter was minimal. The Title II grants, in comparison, are mainly small, and to reduce the certification might impair a district's ability to fund the activities of the grant.

The Chancellor's Office compared each district's 2001-02 first quarter expenditures with the amount of their first quarter apportionment for all VTEA funds. As a result of the analysis, districts were certified at the First Principal Apportionment at 25%, 50%, 75% or 100%. Districts were notified of the changes in the amount certified for apportionment. These notifications can be found at the Vocational Education Services Team (VEST) web site at:

<http://www.cccco.edu/cccco/voced/Resources/2002Memos/2002memos.htm>

VEST Memo 02-06 and 02-06A is the information for the Title IC funds. VEST Memo 02-07 and 02-07A is the information for the Title IB funds. The notification for Title II funds is pending.

These steps should serve as an incentive for districts to report expenditures in an expedient manner.

Language will be added to the Grant Agreement Articles to the effect that "districts must report and pay interest earnings greater than \$100 to the federal awarding agency on any funds that are in excess of the amount received through apportionment." In addition, the Chancellor's Office will issue a memo reminding districts of their responsibility to send interest earnings in excess of \$100 to the federal government and we will have the districts' contracted auditors monitor compliance.

## U.S. DEPARTMENT OF EDUCATION

Federal Catalog Number: 84.048  
Federal Program Title: Vocational Education—Basic Grants to States  
Federal Award Number and  
Calendar Year Awarded: V048A000005A; 2000

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Federal Catalog Number: 84.243  
Federal Program Title: Tech-Prep Education  
Federal Award Number and  
Calendar Year Awarded: V243A000005; 2000

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Reference Number: 2001-5-2  
Federal Catalog Number: 84.126  
Federal Program Title: Rehabilitation Services—Vocational  
Rehabilitation Grants to States  
Federal Award Numbers and  
Calendar Years Awarded: H126A000005; 1999  
H126A010005; 2000  
Category of Finding: Eligibility  
State Administering Department: Department of Rehabilitation

### CRITERIA

Our review of the Rehabilitation Services—Vocational Rehabilitation Grants to States program (Vocational Rehabilitation) determined that the following are among the compliance requirements for eligibility:

The Code of Federal Regulations, Title 34, Section 361.42, requires the State to conduct an assessment for determining an applicant's eligibility and priority for program services. This section further requires the State to base the applicant's eligibility only on a determination that:

- The individual has a physical or mental impairment.
- The impairment substantially impedes employment.

- A presumption that the individual can benefit from program services.
- The individual requires program services to prepare for, secure, or retain employment.

Additionally, Section 361.41 requires the State to determine an individual's eligibility for program services within 60 days of receiving their application, with certain exceptions.

## **CONDITION**

The Department of Rehabilitation (Rehabilitation) does not always determine applicant eligibility for the Vocational Rehabilitation program within the required time period. Of the 32,438 applications received by Rehabilitation from July 1, 2000, through April 30, 2001, Rehabilitation did not determine in 6,260 cases (19 percent) an applicant's eligibility within 60 days or within the time period Rehabilitation and the applicant agreed on when an eligibility-determination extension was used. Rehabilitation was fewer than 10 days late in 38.9 percent of these cases, between 11 and 30 days late in another 30.6 percent of the cases, and between 31 and 60 days late in an additional 17 percent of the cases. Rehabilitation was 61 days or more late in 13.4 percent of the cases. Further, Rehabilitation had not determined eligible or had not closed an additional 1,802 cases as of August 1, 2001. These tardy determinations occurred because although Rehabilitation has the ability to provide district office managers with information on applications that are approaching the deadline for eligibility determinations, it does not do so. When Rehabilitation does not determine an applicant's eligibility within the required time period, it reduces the assurance that clients receive the required rehabilitative services promptly.

## **RECOMMENDATIONS**

To make sure applicants receive program services promptly, Rehabilitation should determine eligibility within the required time period. One approach would be for Rehabilitation to develop "best practices" for its districts to use to approve applications within the required time period and share them with all districts. Also, to help ensure that it determines eligibility timely, Rehabilitation should develop reports, such as aging reports, that show which applications are approaching the eligibility determination deadline. Rehabilitation should provide these reports to supervisors and managers, as necessary, to pinpoint problem areas and help them improve the services Rehabilitation provides to applicants.

## **DEPARTMENT'S VIEW AND CORRECTIVE ACTION PLAN**

Rehabilitation generally agrees with the finding and will consider these recommendations as part of its continuing efforts to streamline and improve the vocational rehabilitation process.

Rehabilitation held a statewide district administrators' meeting in October 2001 and discussed this finding. It is committed to identifying best practices in the determination of eligibility for consumers. Through its preliminary analysis of the causes for the finding, it identified districts that are managing the eligibility-determination process most effectively. Those districts' management practices will be shared with all districts. With the district administrators' input, Rehabilitation is working toward the improvement of the timeliness and accuracy of the management-information reports that are currently available to the districts. Using these reports, Rehabilitation will be able to ensure the consistent use of the management-information reports by the districts to identify consumers who are due for eligibility determination or extension of the eligibility-determination period. For districts that continue to have significant noncompliance issues, Rehabilitation will develop strategies and timelines to resolve the issues.

In addition, based upon recommendations received from its Continuous Improvement Workgroup, Rehabilitation will provide counselors with training that focuses on eligibility determination, specifically as it relates to an applicant's ability to benefit from an employment outcome and the requirements under federal regulation.

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Reference Number:	2001-9-3
Federal Catalog Number:	84.048
Federal Program Title:	Vocational Education—Basic Grants to States
Federal Award Number and Calendar Year Awarded:	V048A000005A; 2000
Category of Finding:	Suspension and Debarment
State Administering Department:	Department of Education

## **CRITERIA**

Our review of the Vocational Education—Basic Grants to States program (Vocational Education) identified the following requirements related to suspension and debarment:

The Code of Federal Regulations, Title 34, Section 85.225, prohibits the State from contracting with any party that is suspended, debarred, or otherwise ineligible to participate in federal assistance programs. In addition, Section 85.510 mandates the State to require certifications from participating organizations affirming that they are not suspended, debarred, ineligible, or voluntarily excluded from transactions by any

federal agency. Further, Section 85.110 makes procurement contracts for goods or services expected to equal or exceed \$100,000 subject to the suspension and debarment certification requirements.

## **CONDITION**

The Department of Education (Education) did not obtain the required suspension and debarment certifications from six of eight contractors we reviewed. Education awarded these participants of the Vocational Education program procurement contracts of \$100,000 or more. According to Education, it did not obtain these certifications because its employees were unaware of the requirements as they relate to vendors. When Education does not obtain the required certifications, it risks unknowingly allowing suspended or debarred parties to participate in the Vocational Education program. For the transactions we reviewed, we used an alternative test to determine that these participants were not on the federal suspended or debarred list.

## **RECOMMENDATION**

Education should ensure that Vocational Education participants receiving procurement contracts of \$100,000 or more submit the required suspension and debarment certification before Education approves their participation in the Vocational Education program.

## **DEPARTMENT'S VIEW AND CORRECTIVE ACTION PLAN**

The required form [Certifications Regarding Lobbying; Debarment, Suspension and other Responsibility Matters; and Drug-Free Workplace Requirements] was mailed to each of the affected contractors for the required signature and return. Education will file the returned forms with the appropriate procurement agreements.

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Reference Number:	2001-9-4
Category of Finding:	Suspension and Debarment
State Administering Department:	Department of Education

(See listing of the specific federal program details following the discussion of the issues below.)

## **CRITERIA**

Our review of federal programs identified the following requirements related to suspension and debarment:

The Code of Federal Regulations, Title 34, Section 85.225, prohibits the State from knowingly doing business with any party that is suspended, debarred, or otherwise ineligible to participate in federal assistance programs. Further, Section 85.510 mandates the State to require a certification from organizations submitting proposals certifying that neither the organization nor its principals are presently debarred, suspended, proposed for debarment, declared ineligible, or voluntarily excluded from participation in federal assistance programs by a federal agency.

## **CONDITION**

The Department of Education (Education) needs to improve its procedures for obtaining the required suspension and debarment certifications. Specifically, Education did not require local education agencies (LEAs) applying to participate in the Title I Grants to Local Educational Agencies program (Title I, Part A) and the Class Size Reduction program to submit the required suspension and debarment certifications. Instead, Education required LEAs to assure that they had complied with the certification requirement. According to Education, the certifications are maintained at the LEA offices and Education reviews these certifications during its site reviews. However, Education only conducts site reviews of LEAs on a four-year cycle; therefore, it cannot annually review each LEA's certification. Thus, although it requires LEAs to apply for program funding annually, Education cannot demonstrate that LEAs made the required certification before it approved their participation in the program.

When Education does not require participants in the Title I, Part A and Class Size Reduction programs to submit the required certification when they apply for program funding, it risks unknowingly allowing suspended or debarred parties to participate in the federal programs. For the transactions we reviewed, we used an alternative test to determine that these program participants were not on the federal suspended or debarred list.

## **RECOMMENDATION**

Education should establish procedures that require participants in the Title I, Part A and Class Size Reduction programs to submit the required suspension and debarment certification before it approves their participation in the programs.

## DEPARTMENT'S VIEW AND CORRECTIVE ACTION PLAN

The Consolidated Application, Part 1 for school year 2002-2003 will be revised and sent to LEAs in April 2002. The revised Consolidated Application will require the LEAs that apply for funding through the Consolidated Application to submit the following statement of assurance:

"The LEA certifies that neither it, nor its principals is presently debarred, suspended, proposed for debarment, declared ineligible, or voluntarily excluded from participation by any Federal department or agency."

### U.S. DEPARTMENT OF EDUCATION

Federal Catalog Number:	84.010
Federal Program Title:	Title I Grants to Local Educational Agencies
Federal Award Number and Calendar Year Awarded:	S010A000005; 2000

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Federal Catalog Number:	84.340
Federal Program Title:	Class Size Reduction
Federal Award Number and Calendar Year Awarded:	S340A000005A; 2000

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Reference Number:	2001-12-2
Category of Finding:	Reporting
State Administering Department:	Department of Education

(See listing of the specific federal program details following the discussion of the issues below.)

### CRITERIA

Our review of the Migrant Education—Basic State Grant Program (Migrant Education) and the Title I Grants to Local Educational Agencies program (Title I, Part A) identified the following requirements related to reporting of school fiscal and student attendance data:

The United States Code, Title 20, sections 6333 and 6393, provide for the use of state average per-pupil expenditures (per-pupil expenditures) in determining the program funds the federal government allocates to states. The National Center for Education Statistics (center) issues instructions on how states are to report data in the National Public Education Financial Survey report (fiscal report) that the center uses to calculate per-pupil expenditures. The center divides the reported state net current expenditures by the reported average daily attendance (ADA) to calculate per-pupil expenditures. The center's instructions specify two methods for states to use when reporting ADA in the fiscal report. Method A requires states to report ADA as defined by state laws or regulations. Method B, which must be used if states do not have laws or regulations defining ADA, requests states to use the center's definition of ADA, which includes summer school ADA.

## **CONDITION**

The Department of Education (Education) did not report the correct ADA in its 1999 fiscal report. Specifically, Education used method A when it reported total ADA in the 1999 fiscal report it submitted to the center. Although it excluded the summer school ADA from the total ADA it reported, Education could not demonstrate which state laws or regulations allow it to exclude summer school ADA from the calculation of total ADA. As a result of Education's omission, it overstated California's per-pupil expenditures by approximately \$122.

According to Education, it excluded the summer school ADA from total ADA because California is moving toward a seamless instructional calendar, and including the summer school ADA would double-count students who are served throughout the year in a variety of circumstances. However, the center's position is that excluding summer school ADA may falsely inflate the State's reported per-pupil expenditures. The center noted that per-pupil expenditures have a direct impact on the federal allocations to states, and that reporting inaccuracies may result in the federal government seeking to recover overpayments. The center estimates that the federal government overpaid California more than \$400,000 because of Education's underreporting of ADA in its 1999 fiscal report.

When Education underreports ADA in its fiscal reports, it risks receiving and spending federal program funds that the federal government may later ask California to repay.

## **RECOMMENDATIONS**

Education should include summer school ADA in the total ADA that it reports and that the federal government uses to calculate California's per-pupil expenditures. In addition, Education should work with the federal awarding agency to resolve any fiscal effects from its inflated fiscal year 1998-99 per-pupil expenditures.



## DEPARTMENT'S VIEW AND CORRECTIVE ACTION PLAN

Education included summer school average daily attendance (ADA) in the subsequent year's 1999-2000 fiscal report, and will work with the federal awarding agency to resolve any fiscal effects of excluding summer school ADA from the 1998-1999 fiscal report. In May 2000, Education wrote to the Acting Commissioner of Education Statistics stating reasons why summer school ADA should be excluded.

### U.S. DEPARTMENT OF EDUCATION

Federal Catalog Number: 84.010  
Federal Program Title: Title I Grants to Local Educational Agencies  
Federal Award Number and  
Calendar Year Awarded: S010A000005; 2000

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Federal Catalog Number: 84.011  
Federal Program Title: Migrant Education—Basic State  
Grant Program  
Federal Award Number and  
Calendar Year Awarded: S011A000005; 2000

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Reference Number: 2001-12-3  
Federal Catalog Number: 84.048  
Federal Program Title: Vocational Education—Basic Grants  
to States  
Federal Award Number and  
Calendar Year Awarded: V048A000005A; 2000  
Category of Finding: Reporting  
State Administering Department: Department of Education

## **CRITERIA**

Our review of the Vocational Education—Basic Grants to States program (Vocational Education) identified the following requirement related to performance reports:

The United States Code, Title 20, Section 2323(c), requires the State to prepare and submit an annual report containing data as to whether it met its adjusted performance levels for each of four core indicators of performance and any state indicators of performance.

## **CONDITION**

The Department of Education (Education) did not report accurate, complete, and supported data in its Vocational Education performance accountability report. To prepare its accountability report, Education obtains performance data from local educational agencies (LEAs) and enters this data into a database it has established to compile the statewide information it reports in its accountability report. However, for 19 of the 35 LEAs we reviewed, Education's entry of LEA data into its database was either inaccurate or incomplete, resulting in Education reporting unreliable information. Education also misreported the total for one core indicator that assesses the State's performance. According to Education, this was its first attempt to prepare this new report, and because of initial flaws in both its data-gathering mechanisms and data-entry procedures, it made errors. When Education does not compile and report accurate and complete data, the U.S. Department of Education cannot accurately assess the State's performance in the Vocational Education program.

## **RECOMMENDATIONS**

Education should implement procedures to ensure that all LEAs submit data, that the data it enters into its database is accurate and complete, and that the information it reports in its Vocational Education performance report is supported.

## **DEPARTMENT'S VIEW AND CORRECTIVE ACTION PLAN**

The forms developed for LEA use in collecting and reporting the required enrollment, completion, and placement data have been rewritten with improved instructions and clearer definitions. Education is assisting LEAs with the implementation of electronic systems for collecting and reporting the required Consolidated Annual Performance, Accountability and Financial Status Report information. Education is also developing a system for electronically receiving and aggregating the enrollment, completion and placement data submitted by the LEAs. This system will be operational by October 2002.

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Reference Number: 2001-14-3  
Category of Finding: Special Tests and Provisions  
State Administering Department: Department of Education

(See listing of the specific federal program details following the discussion of the issues below.)

## **CRITERIA**

Our review of the Migrant Education—Basic State Grant Program (Migrant Education) and the Title I Grants to Local Educational Agencies program (Title I, Part A) determined that the following compliance requirements relate to the comparability of school services:

The United States Code, Title 20, sections 6322(c) and 6394(c), requires local educational agencies (LEAs) that receive Migrant Education and Title I, Part A funds to use state and local funds to provide school services that are at least comparable to services provided by schools not receiving these federal funds, unless otherwise excluded. Furthermore, these sections state that an LEA will have met the requirement of comparability if the LEA has filed with the State education agency a written assurance that the LEA has established and implemented an LEA-wide salary schedule; a policy to ensure equivalence among schools in teachers, administrators, and other staff; and a policy to ensure equivalence among schools in the provision of curriculum materials and instructional supplies.

## **CONDITION**

The Department of Education (Education) did not require LEAs receiving Migrant Education and Title I, Part A funds to file with Education a specific written assurance stating that the LEAs have established and implemented an LEA-wide salary schedule; a policy to ensure equivalence among schools in teachers, administrators, and other staff; and a policy to ensure equivalence among schools in the provision of curriculum materials and instructional supplies. Instead, Education required each LEA to agree to follow standard legal assurances for the respective programs. However, these assurances fall short of the written assurance specified by federal law.

The Migrant Education legal assurance specified for LEAs the comparability requirements, but did not require LEAs to submit a written assurance. The Title I, Part A legal assurance stated, “the LEA has developed and implemented procedures for compliance with the comparability requirements and the compliance documents are updated biannually.” However, this assurance does not state that the LEA has actually established and implemented the specific policies and procedures that federal law requires to ensure comparable school services. Moreover, Education instructed

LEAs to keep these legal assurances on file and not submit them to Education. In addition, although Education reviews local policies during its LEA site visits, it only reviews each LEA on a four-year cycle, and the review instrument it uses does not specify reviewing the policies and procedures to ensure comparable school services. Therefore, Education cannot be sure that LEAs have established and implemented the policies and procedures federal law requires to ensure comparable school services.

When Education does not require LEAs to assure to it in writing that they have implemented specific policies and procedures for using state and local funds to provide school services that are at least comparable to the services provided by schools not receiving Migrant Education and Title I, Part A funds, it cannot be sure that LEAs are using these federal program funds to provide educationally disadvantaged students the additional assistance they need to achieve academic success.

We reported similar findings in our audits of fiscal years 1998-99 and 1999-2000 for these programs. At the time, Education stated it would continue to work with the U.S. Department of Education (USDE) to resolve a similar finding for the Title I, Part A program that the USDE identified in a 1998 Integrated Review report. Further, Education stated that once the comparability issue was satisfactorily resolved for Title I, Part A, it would also be resolved for all Title I programs, including Migrant Education. Although Education has communicated and emphasized the importance of the comparability requirement to LEAs, it has not yet resolved this issue with the USDE.

## **RECOMMENDATIONS**

Education should require LEAs to file with Education written assurances stating that the LEAs have established and implemented the specific policies and procedures federal law requires to ensure they use state and local funds to provide comparable services to all their schools. Additionally, Education should continue to work with the USDE about how Education should revise its monitoring process to ensure that LEAs comply with the comparability requirement.

## **DEPARTMENT'S VIEW AND CORRECTIVE ACTION PLAN**

The Consolidated Application, Part 1 for school year 2002-2003 will be revised, and sent to the LEAs in April 2002. The revised Consolidated Application will require the LEAs that apply for funding through the Consolidated Application to submit the following statement of assurance:

“The LEA has established and implemented a district-wide salary schedule; a policy to ensure equivalence among schools in teachers, administrators, and other staff; and a policy to ensure equivalence among schools in the provision of curriculum materials and instructional supplies.”

In addition to the assurance above, Education will submit a letter to the districts reminding them of their obligations under Title I, Part A Section 1120(c)(2, 3, 4, 5).

Education will continue to work with the U.S. Department of Education to determine the expectation for monitoring this effort.

**U.S. DEPARTMENT OF EDUCATION**

Federal Catalog Number:	84.010
Federal Program Title:	Title I Grants to Local Educational Agencies
Federal Award Number and Calendar Year Awarded:	S010A000005; 2000

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Federal Catalog Number:	84.011
Federal Program Title:	Migrant Education—Basic State Grant Program
Federal Award Number and Calendar Year Awarded:	S011A000005; 2000

**U.S. DEPARTMENT OF EDUCATION**  
**U.S. DEPARTMENT OF HEALTH AND HUMAN SERVICES**

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Reference Number: 2001-8-2

Category of Finding: Period of Availability

State Administering Department: Department of Alcohol and Drug Programs

(See listing of the specific federal program details following the discussion of the issues below.)

**CRITERIA**

Our review of federal programs identified the following compliance requirements relating to period of availability:

The Code of Federal Regulations, Title 34, Section 76.709(a), mandates that if the State does not obligate all of its Safe and Drug-Free Schools and Communities—State Grants (Safe and Drug-Free Schools) program funds by the end of the 15-month funding period for which they were appropriated, the State may obligate the remaining funds for one additional year. In addition, Section 80.23(b) requires the State to liquidate all obligations incurred under an award no later than 90 days after the end of the funding period, which means the State has two years and six months to liquidate its obligations.

Additionally, the United States Code, Title 42, Section 300x-62, requires the State to obligate any Substance Abuse Prevention and Treatment Block Grant amounts by the end of the fiscal year in which the amounts are awarded; and if obligated, spend these amounts by the end of the next fiscal year.

**CONDITION**

The Department of Alcohol and Drug Programs (DADP) lacks adequate procedures to ensure that federal grant awards are obligated and spent within their applicable periods of availability. DADP charged at least \$235,357 against Safe and Drug-Free Schools awards that were not available to DADP at the time. Also, DADP charged at least \$577,441 against Substance Abuse Prevention and Treatment Block Grant awards outside the periods of availability.

Specifically, during fiscal year 2000-01, DADP charged \$89,000 to a Safe and Drug-Free Schools grant award for services that likely occurred before the award was available for obligation and expenditure. Additionally, DADP inappropriately charged at least \$146,357 to a Safe and Drug-Free Schools award for services billed or provided after the grant award had expired. Similarly, for the Substance Abuse Prevention and Treatment Block Grant program, DADP charged at least \$116,716 to a

grant award for services that were provided after the award's period of availability had expired. Furthermore, because DADP did not correctly update the coding in its automated accounting system, it allocated at least \$460,725 of costs to incorrect Substance Abuse Prevention and Treatment Block Grant awards. When DADP does not ensure it charges expenditures only to appropriate and available grant awards, it risks making expenditures for which the federal government may decide not to reimburse it.

Finally, DADP has not fully implemented procedures to reconcile its Substance Abuse Prevention and Treatment Block Grant award expenditures with the grant award fund transfers reflected on the federal awarding agency's Payment Management System. When DADP does not reconcile its expenditures and federal fund transfers for each grant award, it cannot adequately track and be sure it uses the grant award funds before their availability period expires.

## **RECOMMENDATIONS**

DADP should strengthen its procedures to ensure it obligates and expends funds only during each grant award's period of availability. In addition, DADP should continue to implement procedures to reconcile grant award expenditures with the corresponding grant award fund transfers it receives from the federal awarding agency. Finally, DADP should determine appropriate adjustments to its accounting records and refund to the federal awarding agencies any Safe and Drug-Free Schools program funds and Substance Abuse Prevention and Treatment Block Grant program funds that it inappropriately spent outside the applicable periods of availability.

## **DEPARTMENT'S VIEW AND CORRECTIVE ACTION PLAN**

DADP is continuing to improve its procedures for ensuring that obligations and expenditures are recorded only during each grant award's period of availability. Training is being provided to both fiscal and program staff to enhance their understanding of the period of availability for each grant award.

A format for the reconciliation of expenditures and grant transfers has been developed and a regular, monthly reconciliation has been fully implemented for the Safe and Drug-Free Schools program grants. The significantly higher volume of activity in the Substance Abuse Prevention and Treatment Block Grant program has required a longer period of research and will be implemented by July 1, 2002.

DADP is reviewing its accounting records to determine if items identified as outside the period of availability could appropriately be charged to a current award. Once the appropriate adjustments are made, any remaining funds for which the expenditures fall outside the period of availability will be returned to the granting agency.

**U.S. DEPARTMENT OF EDUCATION**

Federal Catalog Number: 84.186

Federal Program Title: Safe and Drug-Free Schools and  
Communities—State Grants

Federal Award Numbers and  
Calendar Years Awarded: S186B70005; 1997  
S186B990005; 1999

**U.S. DEPARTMENT OF HEALTH AND HUMAN SERVICES**

Federal Catalog Number: 93.959

Federal Program Title: Substance Abuse Prevention and  
Treatment Block Grant

Federal Award Numbers and  
Calendar Years Awarded: 98B1CASAPT; 1997  
99B1CASAPT; 1998  
00B1CASAPT; 1999



## **U.S. DEPARTMENT OF HEALTH AND HUMAN SERVICES**

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Reference Number: 2001-3-1

Federal Catalog Number: 93.917

Federal Program Title: HIV Care Formula Grants

Federal Award Numbers and  
Calendar Years Awarded: 5X07HA00041-10; 2000  
2X07HA00041-11; 2001

Category of Finding: Cash Management

State Administering Department: Department of Health Services

### **CRITERIA**

Our review of the HIV Care Formula Grants program identified the following compliance requirements related to cash management:

The Code of Federal Regulations, Title 31, Part 205, Subpart B, provides the cash management requirements for programs not covered in the Cash Management Improvement Act agreement between the U.S. Department of the Treasury and the State. Section 205.20 of this subpart requires the State to limit the cash advances from the U.S. Department of the Treasury to the minimum amounts needed. The subpart also requires the State to time the advances, as close as it can, with its actual and immediate cash needs to carry out the program.

### **CONDITION**

The Department of Health Services (Health Services) did not always minimize the amount of time elapsing between the transfer of federal funds to the State and the funds' disbursement for program costs. Specifically, the time between the receipt of federal funds and the issuance of warrants in 12 of 40 transactions we reviewed ranged from 5 to 23 days. For 7 of those transactions, the elapsed time was 10 days or more. When Health Services does not minimize the amount of time between the receipt and disbursement of federal funds, the State improperly earns interest while federal funds are held in state accounts. For the 12 transactions, we estimate that the State earned about \$2,200 in interest.

## RECOMMENDATION

To minimize the time elapsing between the receipt and disbursement of federal funds, Health Services should request federal funds closer to the date that warrants for program costs are released.

## DEPARTMENT'S VIEW AND CORRECTIVE ACTION PLAN

Health Services agrees with the finding. It also notes that the Cash Management Improvement Act (CMIA) agreement between the U.S. Treasury and the State for fiscal year 2001-02 identifies the HIV Care Formula Grants program as being subject to the tracking and reporting requirements of the CMIA. Health Services states that it will comply with federal requirements.

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Reference Number:	2001-3-4
Federal Catalog Number:	93.568
Federal Program Title:	Low-Income Home Energy Assistance
Federal Award Number and Calendar Year Awarded:	G-00B1CALIEA; 1999
Category of Finding:	Cash Management
State Administering Department:	Department of Community Services and Development

## CRITERIA

Our review of the Low-Income Home Energy Assistance program determined that the following are among the compliance requirements for cash management:

The Code of Federal Regulations, Title 31, Part 205, Subpart B, provides the cash management requirements for programs not covered in the Cash Management Improvement Act agreement between the U.S. Department of the Treasury and the State. Section 205.20 of this subpart requires the State to limit the cash advances from the U.S. Department of the Treasury to the minimum amounts needed. The subpart also requires the State to time the advances, as close as it can, with its actual and immediate cash needs to carry out the program.

## **CONDITION**

The Department of Community Services and Development (Community Services) did not always minimize the amount of time elapsing between the transfer of federal funds to the State and the funds' disbursement for Low-Income Home Energy Assistance program costs. Specifically, the time between receipt of federal funds and the issuance of warrants in 34 of the 40 transactions we reviewed ranged from 4 to 12 days. Four of these transactions took 10 days or more. When Community Services does not minimize the amount of time between the receipt and disbursement of federal funds, the State improperly earns interest on federal funds held in state accounts. For the 34 transactions, we estimate that the State earned approximately \$7,700 in interest.

## **RECOMMENDATION**

To minimize the time elapsing between the receipt and disbursement of federal funds, Community Services should request federal funds closer to the date that warrants for program costs are released.

## **DEPARTMENT'S VIEW AND CORRECTIVE ACTION PLAN**

Community Services recognized this situation and during June 2001 entered into an interagency agreement with the State Controller's Office (SCO) allowing it to pay an additional \$25 to expedite the payment of each claim schedule sent to the SCO. This will ensure that disbursements are made within seventy-two hours after receipt of federal funds. The agreement will allow Community Services to further its efforts in minimizing the time elapsing between the receipt and disbursement of federal funds.

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Reference Number:	2001-3-6
Federal Catalog Number:	93.658
Federal Program Title:	Foster Care—Title IV-E
Federal Award Number and Calendar Year Awarded:	0001CA1401; 1999
Category of Finding:	Cash Management, Reporting
State Administering Department:	Department of Social Services

## **CRITERIA**

Our review of the Foster Care—Title IV-E (Foster Care) program identified the following requirements for cash management and reporting:

The Code of Federal Regulations, Title 45, Section 74.21, requires the State to maintain accurate accounting records and to properly track and report financial activities related to federal grants. This section also requires the State to minimize the time between the transfer of funds from the U.S. Treasury and the disbursement of these funds for program purposes. Additionally, this section requires the State's payment methods to be consistent with the Cash Management Improvement Act Treasury-State Agreement (CMIA Treasury-State Agreement) when applicable. For programs covered under a CMIA Treasury-State Agreement, the State owes the federal government interest from the time the State deposits federal funds in a state account until the State pays the funds for program purposes.

## **CONDITION**

The Department of Social Services (Social Services) overstated its disbursements by more than \$1 million and understated its cash on hand by the same amount for its Foster Care program on the federal cash transaction report to the federal government. Most of this amount—more than \$983,000—represents excess cash Social Services drew down from the U.S. Treasury on July 28, 2000. The remaining amount, more than \$27,000, represents unused funds returned by a county on February 9, 2001. Social Services erroneously reported this cash on hand as disbursements. When Social Services does this, it overstates the amount of federal funds spent on program purposes and understates the amount of cash it has on hand to meet program needs.

Additionally, although the program is covered by the CMIA Treasury-State Agreement, Social Services did not report to the Department of Finance (Finance), the state agency responsible for calculating the State's interest liability, the correct information reflecting how long it was maintaining this cash balance. As a result, Finance calculates that the State's interest liability for the Foster Care program was understated by more than \$55,000.

## **RECOMMENDATIONS**

Social Services should ensure that it accurately reports disbursements and cash on hand in its federal cash transaction reports. Additionally, it should monitor its cash balances for its federal programs and ensure that it requests only the federal cash necessary to meet its immediate program needs.

## DEPARTMENT'S VIEW AND CORRECTIVE ACTION PLAN

Social Services concurs. Social Services realizes the importance of monitoring its cash balances given that it disburses approximately \$7 billion in federal funds annually. Social Services is now directing more focus to monitoring cash-on-hand at the State Controller's Office and on following up to ensure staff uses cash for program purposes within a reasonable period of time. Social Services will also review its reporting procedures for the cash transaction report and for its CMIA agreement to ensure they are consistent with federal reporting requirements.

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Reference Number:	2001-7-1
Federal Catalog Number:	93.994
Federal Program Title:	Maternal and Child Health Services Block Grant to the States
Federal Award Numbers and Calendar Years Awarded:	6B04MC00336-03; 1999 6B04MC00336-04; 2000
Category of Finding:	Earmarking
State Administering Department:	Department of Health Services

### CRITERIA

Our review of the Maternal and Child Health Services Block Grant to the States program (program) determined that the following compliance requirements apply to earmarking:

The United States Code, Title 42, Section 705(a)(3), requires states generally to use at least 30 percent of program payments for preventative and primary health care for children, and at least 30 percent for services for children with special health care needs. In addition, Section 704(d) prohibits states from using more than 10 percent of the annual grant amount to administer the program's funds.

### CONDITION

The Department of Health Services (Health Services) does not have adequate procedures to ensure that it meets the program's earmarking requirements. As a result, it cannot be sure that children received sufficient levels of service and that it spent federal funds in compliance with federal requirements. Rather than reflecting in its accounting system the actual amounts spent for each of the three earmarked

components, Health Services uses predetermined percentages to allocate subrecipient and contractor payments to these areas. Health Services believes that requiring contractors to report actual amounts spent on each type of individual served and by service provided would create undue administrative hardships.

## **RECOMMENDATION**

Health Services should obtain formal approval from the federal government of the procedures it uses for calculating how it meets the earmarking requirements.

## **DEPARTMENT'S VIEW AND CORRECTIVE ACTION PLAN**

Health Services agrees that it uses predetermined percentages to estimate the amounts spent for each of the required program components. It also believes that using estimates is the most viable approach to spreading costs to these components. Health Services states that the assigned percentages are based on the target population. It also based them on the program activities that are established by legislative authorization and specified in the scope of work for each contractor.

Health Services states that it has informally contacted the federal Maternal and Child Health Bureau (federal bureau) regarding its interpretation of this requirement and how other states implement the 30-30-10 allocation. According to Health Services, the federal bureau said that it does not routinely review the methodology states use to meet the earmarking requirements. Health Services asserts that if based upon this finding the federal bureau determines that California is not in compliance with this requirement, Health Services will work directly with the federal bureau to address this issue administratively rather than place the burden on local contractors.

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Reference Number:	2001-7-2
Federal Catalog Number:	93.778
Federal Program Title:	Medical Assistance Program
Federal Award Numbers and Calendar Years Awarded:	05-0005CA5028; 1999 05-0105CA5028; 2000
Category of Finding:	Matching
State Administering Department:	Department of Health Services

## **CRITERIA**

Our review of the Medical Assistance Program (Medicaid) identified the following compliance requirements related to matching:

Under the United States Code, Title 42, Section 1396 et seq. and related federal regulations, the federal government will pay a portion of the claims for allowable costs of services provided to eligible individuals. The Department of Health Services (Health Services) reviews Medicaid claims from service providers and then obtains federal funds to cover the federal government's portion of approved costs. From October 1, 1999, through September 30, 2000, the applicable federal portion for California was 51.67 percent. From October 1, 2000, through September 30, 2001, the rate was 51.25 percent.

## **CONDITION**

Health Services does not always apply the correct federal rate for Medicaid claims. Specifically, for \$582.6 million in claims filed during fiscal year 2000-01 for services provided between October 1, 2000, and June 30, 2001, Health Services applied a rate of 51.67 percent rather than the approved rate of 51.25 percent. As a result, Health Services overcharged the federal government nearly \$2.4 million for its share of the claims. Health Services used the incorrect rate because its staff neglected to update the rate at the start of the new federal fiscal year, and management's review did not identify the discrepancy.

## **RECOMMENDATIONS**

Health Services should ensure that it applies the correct federal rate when drawing down federal funds for Medicaid claims. Further, it should identify claims that it incorrectly processed, recalculate the proper amount that the federal government should have paid, and reimburse the federal government for the overpayments.

## **DEPARTMENT'S VIEW AND CORRECTIVE ACTION PLAN**

Health Services concurs with the finding. It stated that it would implement a new procedure for communicating updated Medicaid rates to its staff. Further, Health Services stated that it will ensure that any overpayments of federal funds are offset by other fund sources when it closes out its accounting for fiscal year 2000-01. If an overpayment remains after closure, Health Services will reimburse the federal government.

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Reference Number: 2001-9-2  
Category of Finding: Suspension and Debarment  
State Administering Department: Department of Health Services

(See listing of the specific federal program details following the discussion of the issues below.)

## **CRITERIA**

Our review of federal programs identified the following compliance requirements related to suspension and debarment:

The Code of Federal Regulations, Title 45, Section 76.225, prohibits the State from knowingly doing business with any party that is suspended, debarred, or otherwise ineligible to participate in federal assistance programs. Further, Section 76.510 requires the State to obtain signed certifications from participating organizations regarding debarment, suspension, ineligibility, and voluntary exclusion.

## **CONDITION**

The Department of Health Services (Health Services) did not always obtain the required suspension and debarment certifications from its subrecipients during fiscal year 2000-01. Specifically, it did not require the certifications from the 32 subrecipients that we reviewed that participated in the Immunization Grants program, nor from the 10 subrecipients that we reviewed who participated in the HIV Care Formula Grants program. Further, Health Services failed to obtain the suspension and debarment certifications from 3 of the 15 subrecipients that we reviewed that participated in the Maternal and Child Health Services Block Grant to the States program. When Health Services does not obtain the required certifications, it risks unknowingly allowing suspended or debarred parties to participate in the federal programs. For the transactions we reviewed, we used an alternative test to determine that these participants were not suspended or debarred.

As part of our work, we reviewed the contracts used by the Immunization Grants and HIV Care Formula Grants programs for fiscal year 2001-02. We observed that these programs included a suspension and debarment certification as part of their newer contracts.

## **RECOMMENDATION**

Health Services should ensure that it obtains suspension and debarment certifications from all subrecipients of federal program funds.



## DEPARTMENT'S VIEW AND CORRECTIVE ACTION PLAN

Health Services concurs with the finding. Although Health Services has developed a procedure for obtaining the required suspension and debarment certifications, it is in the early stages of implementation. To ensure that all certifications are obtained and that it follows its procedures, Health Services plans to coordinate with other branches in the department that receive federal program funds to ensure that they include the correct language and follow updated procedures.

### U.S. DEPARTMENT OF HEALTH AND HUMAN SERVICES

Federal Catalog Number:	93.268
Federal Program Title:	Immunization Grants
Federal Award Numbers and Calendar Years Awarded:	H23/CCH904423-10-15; 1999 H23/CCH904423-11-8; 2001
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Federal Catalog Number:	93.917
Federal Program Title:	HIV Care Formula Grants
Federal Award Numbers and Calendar Years Awarded:	5X07HA00041-10; 2000 2X07HA00041-11; 2001
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Federal Catalog Number:	93.994
Federal Program Title:	Maternal and Child Health Services Block Grant to the States
Federal Award Numbers and Calendar Years Awarded:	6B04MC00336-03; 1999 6B04MC00336-04; 2000
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Reference Number:	2001-12-1
Federal Catalog Number:	93.994
Federal Program Title:	Maternal and Child Health Services Block Grant to the States
Federal Award Numbers and Calendar Years Awarded:	6B04MC00336-03; 1999 6B04MC00336-04; 2000

Category of Finding:

Reporting

State Administering Department:

Department of Health Services

## **CRITERIA**

Our review of the Maternal and Child Health Services Block Grant to the States program (program) determined that the following compliance requirements apply to reporting:

The United States Code, Title 42, Section 706(a), requires the State to prepare and submit an annual report concerning its program activities. This annual report must contain accurate information pertaining to the description of such activities, a complete record of the purposes for which the funds were spent, and a description of the extent to which the State has met certain program goals. Additionally, federal guidelines for completing the report instruct the State to make an estimate if an actual number is unavailable and to explain all estimates in a footnote.

## **CONDITION**

The Department of Health Services (Health Services) does not always report complete information in its annual program report to the U.S. Department of Health and Human Services (HHS). Specifically, Health Services does not identify and explain that it estimated some of the expenditures and other amounts in its annual report. For example, although Health Services reported spending \$1.12 billion for fiscal year 1998-99 program activities, it did not identify and explain that it derived this amount using estimates for several program components, including \$374.5 million from its Children's Medical Services Branch. Additionally, Health Services used predetermined percentages to estimate certain expenditures by the types of individuals served and by the types of services provided. Similarly, because it used a flawed methodology, Health Services submitted an incorrect estimate of the number of HIV cases in California needing and receiving treatment. To estimate this number, Health Services multiplied its estimation of the number of confirmed HIV cases in California by a percentage that bears no relationship to the population the department was attempting to identify. Further, in reporting the primary sources of insurance coverage for infants less than 1 year of age and for children 1 to 22 years of age, Health Services used data from its Child Health and Disability Prevention program report that was based upon estimates. Finally, in reporting the primary sources of insurance coverage for children with special health care needs, Health Services used average caseloads from county administrative claims to estimate the number of children served.

When Health Services does not identify and explain all estimates that it uses in its annual report to the federal government, HHS may be unable to make a sound assessment of its success in enhancing the well-being of mothers and children served by the program.

As part of our work, we also reviewed Health Services' annual report for the next fiscal year—1999-2000. We observed that Health Services added new footnotes explaining its use of estimates to derive some expenditures and other amounts. It also ceased estimating the number of HIV cases in California that needed and received treatment. However, Health Services' use of other estimates continues to be unexplained.

## **RECOMMENDATION**

Health Services should identify and explain all estimates it uses in its annual report to HHS.

## **DEPARTMENT'S VIEW AND CORRECTIVE ACTION PLAN**

Health Services agrees with the recommendation. It said that when it prepares future annual reports to the federal government, it will fully disclose and explain all estimates used by the different programs providing input into the report.

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Reference Number:	2001-12-6
Federal Catalog Number:	93.568
Federal Program Title:	Low-Income Home Energy Assistance
Federal Award Number and Calendar Year Awarded:	G-00B1CALIEA; 1999
Category of Finding:	Reporting
State Administering Department:	Department of Community Services and Development

## **CRITERIA**

Our review of the Low-Income Home Energy Assistance program determined that the following are among the compliance requirements for reporting:

The Code of Federal Regulations, Title 45, Section 96.82, requires the State to submit annually to the U.S. Department of Health and Human Services (HHS) the data required by the United States Code, Title 42, Section 8624(c)(1)(G) for the 12-month period corresponding to the federal fiscal year. Under the requirements of Section 8624(c)(1)(G), the State must prepare and submit a plan that reports the number and income levels of households that apply for assistance and the number that are

assisted with federal funds. Further, the State must report the number of households assisted that have one or more members who are at least 60 years of age, have one or more members who are disabled, and have one or more young children.

## **CONDITION**

In its January 2001 report to HHS, the Department of Community Services and Development (Community Services) did not accurately report for the Low-Income Home Energy Assistance program the number of households it served during the federal fiscal period covering October 1, 1999, through September 30, 2000, and the demographics of these households. Specifically, Community Services failed to include in its report the data for services provided during certain periods. The information was mistakenly omitted and Community Services' management review did not detect the omission. As a result, Community Services underreported the services it provided in nearly every category. For example, it understated by at least 1,330 households the number of households assisted under the Home Energy Assistance component of the program.

## **RECOMMENDATION**

Community Services should ensure it accurately reports assistance activity to HHS.

## **DEPARTMENT'S VIEW AND CORRECTIVE ACTION PLAN**

Community Services will take greater care, in the future, to ensure that all information is accurately submitted.

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Reference Number:	2001-14-4
Federal Catalog Number:	93.778
Federal Program Title:	Medical Assistance Program
Federal Award Numbers and Calendar Years Awarded:	05-0005CA5028; 1999 05-0105CA5028; 2000
Category of Finding:	Special Tests and Provisions
State Administering Department:	Department of Health Services

## **CRITERIA**

Our review of the Medical Assistance Program (Medicaid) identified the following compliance requirements related to medical service providers:

The Code of Federal Regulations, Title 42, Section 431.107, requires the State to provide for an agreement between the state agency administering the Medicaid program and each provider. The provider must agree to disclose certain information, including any significant ownership or controlling interest in any other entity that is paid Medicaid funds, as outlined in sections 455.103 through 455.106. Further, Section 455.104 requires providers to update their disclosures when their facilities are surveyed or agreements are renewed.

## **CONDITION**

The Department of Health Services (Health Services) does not have adequate controls over provider agreements. Specifically, our review of 30 provider files revealed that Health Services could not locate agreements for 8 of these providers. Further, although Health Services had on file at least an application for 29 of the 30 providers, it could not locate any disclosure information for one provider. Although we identified a similar weakness during our audit of the prior year, the number of sampled providers with missing documents is lower this year. During our audit of fiscal year 1999-2000, Health Services could not locate agreements for 24 of the 31 providers we reviewed and could not locate any disclosure information for 5 providers.

When Health Services cannot demonstrate that it obtained the required provider agreements and disclosures, it cannot ensure that it made Medicaid claim payments only to authorized providers.

Health Services said it has developed an expanded provider agreement and is continuing the process of re-enrolling existing providers. Because approximately 140,000 providers exist, Health Services prioritized its re-enrollment process and started re-enrolling higher-risk providers in June 1999. Health Services estimates that it has re-enrolled nearly 600 providers and placed another 900 on inactive status.

## **RECOMMENDATION**

Health Services should continue with its re-enrollment process of renewing provider files so that provider agreements, disclosure of significant beneficial interest, and other pertinent provider information is reasonably current.

## DEPARTMENT'S VIEW AND CORRECTIVE ACTION PLAN

Health Services concurs with the finding. It stated that it has instituted the following activities to help resolve the issue:

- Initiated preliminary discussions with the Licensing and Certification Program to incorporate provider agreements into the acute care enrollment process.
- Continue the re-enrollment process so that provider agreements and disclosure of significant beneficial interest are reasonably current. Health Services is currently giving priority to higher-risk providers.
- Place on inactive status those providers that have not billed for services for 12 months.

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Reference Number:	2001-14-5
Federal Catalog Number:	93.778
Federal Program Title:	Medical Assistance Program
Federal Award Numbers and Calendar Years Awarded:	05-0005CA5028; 1999 05-0105CA5028; 2000
Category of Finding:	Special Tests and Provisions
State Administering Department:	Department of Health Services

### CRITERIA

Our review of the Medical Assistance Program (Medicaid) identified the following compliance requirements related to payment rates for service providers:

The Code of Federal Regulations, Title 42, Section 447.253(b)(1), requires Medicaid payments for services provided by long-term care facilities to be based on rates that are reasonable and adequate to meet costs incurred by economically and efficiently operated providers in order to provide services conforming with laws, regulations, and standards. Further, Section 447.253(i) states that the rates must be determined according to the methods and standards specified in the federally approved Medicaid State Plan (state plan). To set reasonable and adequate rates as required by the Code of Federal Regulations, the state plan requires the Department of Health Services (Health Services) to annually perform a rate study. As part of this rate

study, Health Services uses information from cost reports filed by service providers. To verify the accuracy of the amounts reported, the state plan requires Health Services to audit a sample of the cost reports submitted.

## **CONDITION**

When calculating the payment rates effective August 2001 for long-term care facilities that treat developmentally disabled individuals (LTC facilities), Health Services audited far fewer cost reports than it would have audited had it followed its established methodology. Specifically, Health Services audited only 146 cost reports for LTC facilities, 327 fewer reports than the 473 called for based on the state plan and on Health Services' sample-setting methodology. The state plan calls for the sample size to be a minimum of 15 percent of the total number of cost reports submitted and large enough to meet certain statistical expectations (statistical amount). To calculate the statistical amount, Health Services uses a mathematical formula, a portion of which relies on the results of the most recently available cost report audits. For example, when determining the payment rates for use beginning August 2001, Health Services would use the audit results of cost reports covering fiscal periods ending in 1999 in its mathematical formula.

Health Services did not audit its full complement of cost reports for the LTC facilities because, after it calculated the sample size, it concluded that it did not have sufficient staff to perform the work. Rather than obtaining additional resources or requesting approval from the U.S. Department of Health and Human Services to deviate from the state plan's provisions concerning sample size, Health Services subsequently reduced the sample size to 146 by relying on information from cost reports covering an earlier fiscal period. We recognize that for one type of LTC facility, the sample size that Health Services used was more than twice as large as those it used in previous years. For another type of facility, the sample size was comparable to that of previous years.

Because it did not audit the number of cost reports required by the state plan's provisions and according to its past practices, Health Services has less assurance that the rates it developed for LTC facilities are reasonable and adequate to meet costs incurred by service providers. If, for instance, the rates are lower than they otherwise would have been had Health Services performed the required number of cost report audits, service providers will not earn amounts sufficient to cover their costs. On the other hand, if the rates are higher than they otherwise would have been, the state and federal governments could pay service providers more than they should receive. Although Health Services does not believe the reduction in the number of cost report audits performed materially affected rates, it provided no substantive analyses to support its position.

## **RECOMMENDATIONS**

Health Services should determine conclusively whether the number of cost reports from LTC facilities that it audited is large enough to meet the statistical expectations of the state plan. If the sample size is not large enough, Health Services should request approval from the U.S. Department of Health and Human Services to deviate from the state plan's provisions concerning sample size.

## **DEPARTMENT'S VIEW AND CORRECTIVE ACTION PLAN**

With respect to the two types of facilities, Health Services disagrees with the finding that it did not audit the number of cost reports as required by the state plan's provisions and according to its past practices. While Health Services audited fewer cost reports than what was selected, it believes that it complied with the state plan. Specifically, it audited 15 percent of the population of cost reports, and it believes that the state plan can be interpreted to mean that a 15 percent sample is sufficiently large enough to reasonably expect audit results and a class audit adjustment factor representative of the class of facilities for which it will be used during the annual rate-setting process. Moreover, Health Services states that the number of cost reports actually audited (146 cost reports), as opposed to the sample size selected (395 cost reports) is significantly higher than the number of cost reports audited in previous years.

Health Services also points out that the class audit adjustment for the one type of LTC facility derived from the sample in question was .9655, whereas the class audit adjustment for the previous year was .93852. The class audit adjustment for the other type of facility derived from the sample in question was .94061, whereas the class audit adjustment for the previous year was .94603. Therefore, Health Services maintains, the adjustments derived from the sample in question were, in effect, within reason. Notwithstanding the above, Health Services is committed to revising, based on the concerns identified in the audit, the language in the state plan addressing the sampling methodology for the selection of facilities to be field-audited.



## **AUDITEE'S SECTION**

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## **Schedule of Federal Assistance**

**Prepared by  
Department of Finance**

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**STATE OF CALIFORNIA  
SCHEDULE OF FEDERAL ASSISTANCE  
FISCAL YEAR ENDED JUNE 30, 2001**

Federal Agency/Program Title	Federal Catalog Number	Grant Amount Received
<b>Department of Agriculture</b>		
Market Protection and Promotion	10.163	111,680
Farm Labor Housing Loans and Grants	10.405	500,000
Rural Housing Preservation Grants	10.433	761,741
Food Distribution	10.550	98,698,357 *
Special Supplemental Food Program for Women, Infants, and Children	10.557	718,343,689
Child and Adult Care Food Program	10.558	194,766,897
State Administrative Expenses for Child Nutrition	10.560	16,069,261
Commodity Supplemental Food Program	10.565	2,298,770
Nutrition Program for the Elderly	10.570	10,824,581
WIC Farmers' Market Nutrition Program (FMNP)	10.572	3,792,670
Team Nutrition Grants	10.574	144,621
Cooperative Forestry Assistance	10.664	1,430,036
National Forest-Dependent Rural Communities	10.670	257,360
Other - U.S. Department of Agriculture	10.999	<u>8,411,606</u>
<b>Total Excluding Clusters</b>		1,056,411,269
<b>Food Stamp Cluster</b>		
Food Stamps	10.551	1,576,288,377 *
State Administrative Matching Grants for Food Stamp Program	10.561	<u>273,988,098</u>
<b>Total Food Stamp Cluster</b>		1,850,276,475
<b>Child Nutrition Cluster</b>		
School Breakfast Program	10.553	196,564,508
National School Lunch Program	10.555	760,939,147
Special Milk Program for Children	10.556	764,910
Summer Food Service Program for Children	10.559	<u>18,302,763</u>
<b>Total Child Nutrition Cluster</b>		976,571,328
<b>Emergency Food Assistance Cluster</b>		
Emergency Food Assistance Program	10.568	5,687,785
Emergency Food Assistance (commodities)	10.569	<u>32,286,554 *</u>
<b>Total Emergency Food Assistance Cluster</b>		37,974,339

Federal Agency/Program Title	Federal Catalog Number	Grant Amount Received
<b>Research &amp; Development Cluster</b>		
Federal-State Marketing Improvement Program	10.156	49,100
Market Protection and Promotion	10.163	23,906
Cooperative Forestry Assistance	10.664	<u>122,392</u>
<b>Total Research &amp; Development Cluster</b>		195,398
<b>Schools and Roads Cluster</b>		
Schools and Roads - Grants to States	10.665	<u>26,422,003</u>
<b>Total U.S. Department of Agriculture</b>		<u>3,947,850,812</u>
<b>Department of Commerce</b>		
Economic Development-Support for Planning Organizations	11.302	150,000
Economic Adjustment Assistance	11.307	199,535
Sudden and Severe Economic Dislocation	11.311	8,889,063 ***
Anadromous Fish Conservation Act Program	11.405	322,880
Interjurisdictional Fisheries Act of 1986	11.407	132,397
Coastal Zone Management Administration Awards	11.419	2,776,968
Coastal Zone Management Estuarine Research Reserves	11.420	564,309
Marine Sanctuary Program	11.429	37,281
Pacific Coast Salmon Recovery-Pacific Salmon Treaty Program	11.438	430,585
Habitat Conservation	11.463	330,560
Office of Administration Special Programs	11.470	31,288
Technology Opportunities	11.552	95,372
Other - U.S. Department of Commerce	11.999	<u>85,716</u>
<b>Total U.S. Department of Commerce</b>		<u>14,045,954</u>
<b>Department of Defense</b>		
Planning Assistance to States	12.110	480,185
State Memorandum of Agreement Program for the Reimbursement of Technical Services	12.113	11,983,871
National Guard Military Operations and Maintenance (O&M) Projects	12.401	40,677,303
Community Economic Adjustment Planning Assistance	12.607	<u>32,903</u>
<b>Total U.S. Department of Defense</b>		<u>53,174,262</u>
<b>Department of Housing and Urban Development</b>		
Manufactured Home Construction and Safety Standards	14.171	167,200
Community Development Block Grants/State's Program	14.228	39,460,473

Federal Agency/Program Title	Federal Catalog Number	Grant Amount Received
Emergency Shelter Grants Program	14.231	5,398,907
Supportive Housing Program	14.235	5,221,949 ***
HOME Investment Partnerships Program	14.239	74,931,819 ***
Housing Opportunities for Persons with AIDS	14.241	2,557,330
Equal Opportunity in Housing	14.400	985,150
Lead-Based Paint Hazard Control Priority Housing	14.900	<u>1,008,236</u>
<b>Total Excluding Clusters</b>		129,731,064
<b>Section 8 Project-Based Cluster</b>		
Lower Income Housing Assistance Program-Section 8 Moderate Rehabilitation	14.856	110,274
<b>Section 8 Tenant-Based Cluster</b>		
Section 8 Rental Voucher Program	14.855	2,795,043
Section 8 Rental Certificate Program	14.857	<u>292,868</u>
<b>Total Section 8 Tenant-Based Cluster</b>		<u>3,087,911</u>
<b>Total U.S. Department of Housing and Urban Development</b>		<u>132,929,249</u>

**Department of the Interior**

Recreation Resource Management	15.225	721
Small Reclamation Projects	15.503	328,048
Anadromous Fish Conservation	15.600	79,470
Endangered Species Conservation	15.612	404,119
Coastal Wetlands Planning, Protection and Restoration Act	15.614	118,984
Cooperative Endangered Species Conservation Fund	15.615	460,950
Clean Vessel Act	15.616	280,000
Wildlife Conservation and Appreciation	15.617	6,476
Administrative Grants for Federal Aid in Sport Fish and Wildlife Restoration	15.618	419,926
Geological Survey-Research and Data Acquisition	15.808	137,454
Historic Preservation Fund Grants-In - Aid	15.904	891,993
Outdoor Recreation-Acquisition, Development and Planning	15.916	1,339,440
National Maritime Heritage Grants	15.925	18,815
Research Information	15.975	895,625
Other - U.S. Department of the Interior	15.999	<u>40,564,316</u>
<b>Total Excluding Clusters</b>		45,946,337
<b>Fish and Wildlife Cluster</b>		
Sport Fish Restoration	15.605	10,596,654
Wildlife Restoration	15.611	<u>5,763,706</u>
<b>Total Fish and Wildlife Cluster</b>		16,360,360

Federal Agency/Program Title	Federal Catalog Number	Grant Amount Received
<b>Research and Development Cluster</b>		
Anadromous Fish Conservation	15.600	11,810
Coastal Wetlands Planning, Protection and Restoration Act	15.614	<u>30,593</u>
<b>Total Research and Development Cluster</b>		<u>42,403</u>
<b>Total U.S. Department of the Interior</b>		<u>62,349,100</u>

**Department of Justice**

State Domestic Preparedness Equipment Support Program	16.007	36,337
Juvenile Accountability Incentive Block Grants	16.523	21,161,257
Juvenile Justice and Delinquency Prevention-Allocation to States	16.540	8,730,860
Juvenile Justice and Delinquency Prevention-Special Emphasis	16.541	2,681,107
Part E-State Challenge Activities	16.549	638,706
National Criminal History Improvement Program	16.554	3,496,761
National Sex Offender Registry Assistance	16.555	282,281
Criminal Justice Discretionary Grant Program	16.574	1,137,478
Crime Victim Assistance	16.575	34,347,876
Crime Victim Compensation	16.576	19,161,000
Byrne Formula Grant Program	16.579	53,508,771
Edward Byrne Memorial State and Local Law Enforcement Assistance Discretionary Grants Program	16.580	31,301
Violent Offender Incarceration and Truth in Sentencing Incentive Grants	16.586	24,987,668
Violence Against Women Formula Grants	16.588	17,625,137
Rural Domestic Violence and Child Victimization Enforcement Grant Program	16.589	242,738
Grants to Encourage Arrest Policies and Enforcement of Protection Orders	16.590	181,964
Local Law Enforcement Block Grants Program	16.592	2,370,968
Residential Substance Abuse Treatment for State Prisoners	16.593	4,912,967
Tuberculosis Prevention Diagnosis and Treatment Program	16.594	35,774
State Identification Systems Grant Program	16.598	115,656
Corrections-Technical Assistance/Clearinghouse	16.603	175,528
State Criminal Alien Assistance Program	16.606	195,851,999
Bulletproof Vest Partnership Program	16.607	490,375
Regional Information Sharing Systems	16.610	2,891,542
Public Safety Partnership and Community Policing Grants ("COPS" Grants)	16.710	11,313,180
Other - U.S. Department of Justice	16.999	<u>1,569,396</u>
<b>Total Excluding Clusters</b>		407,978,627



Federal Agency/Program Title	Federal Catalog Number	Grant Amount Received
<b>Research and Development Cluster</b>		
Violence Against Women Formula Grants	16.588	<u>55,534</u>
<b>Total U.S. Department of Justice</b>		<u>408,034,161</u>
<b>Department of Labor</b>		
Labor Force Statistics	17.002	6,432,336
Compensation and Working Conditions Data	17.005	246,709
Labor Certification for Alien Workers	17.203	5,717,161
Unemployment Insurance	17.225	2,980,142,166
Senior Community Service Employment Program	17.235	7,249,191
Trade Adjustment Assistance-Workers	17.245	10,561,878
Employment Services and Job Training - Pilot and Demonstration Programs	17.249	88,454
Welfare-to-Work Grants to States and Localities	17.253	103,773,722
Workforce Investment Act	17.255	302,822,528
Occupational Safety and Health	17.500	403,635
Occupational Safety and Health-State Program	17.503	22,416,306
Consultation Agreements	17.504	6,230,442
Mine Health and Safety Grants	17.600	248,411
Veterans' Employment Program	17.802	1,244,331
Other-U.S. Department of Labor	17.999	<u>1,167,404</u>
<b>Total Excluding Clusters</b>		3,448,744,674
<b>Employment Services Cluster</b>		
Employment Service	17.207	106,332,702
Disabled Veterans' Outreach Program	17.801	11,843,921
Local Veterans' Employment Representative Program	17.804	<u>6,675,886</u>
<b>Total Employment Services Cluster</b>		124,852,509
<b>JTPA Cluster</b>		
Employment and Training Assist-Dislocated Workers	17.246	75,138,333
Job Training Partnership Act	17.250	<u>67,459,814</u>
<b>Total JTPA Cluster</b>		<u>142,598,147</u>
<b>Total U.S. Department of Labor</b>		<u>3,716,195,330</u>
<b>Department of Transportation</b>		
Boating Safety Financial Assistance	20.005	2,037,209
Airport Improvement Program	20.106	185,062
Motor Carrier Safety	20.217	5,468,441

Federal Agency/Program Title	Federal Catalog Number	Grant Amount Received
Local Rail Freight Assistance	20.308	1,454,013
Federal Transit-Metropolitan Planning Grants	20.505	39,551,167
Public Transportation for Nonurbanized Areas	20.509	11,293,351
Pipeline Safety	20.700	2,358,636
Interagency Hazardous Materials Public Sector Training and Planning Grants	20.703	922,055
Other-U.S. Department of Transportation	20.999	<u>634,597</u>
<b>Total Excluding Clusters</b>		63,904,531
<b>Highway Planning and Construction Cluster</b>		
Highway Planning & Construction	20.205	1,729,993,539 ***
<b>Federal Transit Cluster</b>		
Federal Transit Capital Improvement Grants	20.500	4,587,476
<b>Highway Safety Cluster</b>		
State & Community Highway Safety	20.600	37,359,063
<b>Research and Development Cluster</b>		
Highway Planning & Construction	20.205	<u>21,319,119</u>
<b>Total U.S. Department of Transportation</b>		<u>1,857,163,728</u>
<b>Department of Treasury</b>		
Other -U.S. Department of Treasury	21.999	263,919
<b>Equal Employment Opportunity Commission</b>		
Employment Discrimination-State and Local Fair Employment Practices Agency Contracts	30.002	3,056,850
<b>General Services Administration</b>		
Donation of Federal Surplus Personal Property	39.003	6,866,940 **
<b>National Aeronautics and Space Administration</b>		
Technology Transfer	43.002	105,514
<b>National Foundation on the Arts and the Humanities</b>		
Promotion of the Arts-State and Regional Program	45.007	836,800
State Library Program	45.310	<u>14,972,427</u>
<b>Total National Foundation on the Arts and Humanities</b>		<u>15,809,227</u>

Federal Agency/Program Title	Federal Catalog Number	Grant Amount Received
<b>Small Business Administration</b>		
Small Business Development Center	59.037	8,702,771
<b>Department of Veterans Affairs</b>		
Grants to State for Construction of States Home Facilities	64.005	5,854,987
Veterans State Domiciliary Care	64.014	5,398,941
Veterans State Nursing Home Care	64.015	6,186,853
Veterans State Hospital Care	64.016	119,515
All Volunteer Force Educational Assistance	64.124	54,478
Other-U.S. Department of Veterans Affairs	64.999	<u>959,037</u>
<b>Total U.S. Department of Veteran's Affairs</b>		<u><b>18,573,811</b></u>
<b>Environmental Protection Agency</b>		
Air Pollution Control Program Support	66.001	7,414,911
Air Pollution Control - National Ambient Air and Source Emission Data	66.007	55,263
State Indoor Radon Grants	66.032	213,338
Water Pollution Control-State and Interstate Program Support	66.419	4,084,384
State Underground Water Source Protection	66.433	333,065
Construction Management Assistance	66.438	13,657
Water Quality Management Planning	66.454	708,265
National Estuary Program	66.456	217,727
Capitalization Grants for State Revolving Funds	66.458	1,264,260,908 ***
Nonpoint Source Implementation Grants	66.460	7,112,172
Wetlands Grants	66.461	491,744
Water Quality Cooperative Agreements	66.463	671,686
Near Coastal Waters	66.464	45,266
Capitalization Grants for Drinking Water State Revolving Fund	66.468	77,506,142 ***
Hardship Grants for Rural Communities	66.470	706,455
Safe Drinking Water Research and Demonstration	66.506	3,528,952
Toxic Substances Research	66.507	219,506
Surveys, Studies, Investigations and Special Purpose Grants	66.606	827,913
Consolidated Pesticide Enforcement Cooperative Agreements	66.700	1,192,684
Toxic Substances Compliance Monitoring Cooperative Agreements	66.701	104,319
TSCA Title IV State Lead Grants-Certification of Lead-Based Paint Professionals	66.707	399,862
Pollution Prevention Grants Program	66.708	53,593
Hazardous Waste Management State Program Support	66.801	8,039,588

Federal Agency/Program Title	Federal Catalog Number	Grant Amount Received
Superfund State Site-Specific Cooperative Agreements	66.802	1,968,485
State and Tribal Underground Storage Tanks Program	66.804	370,197
Leaking Underground Storage Tank Trust Fund Program	66.805	2,835,559
Solid Waste Management Assistance	66.808	106,654
CEPP Technical Assistance Grants Program	66.810	50,000
Brownfield Pilots Cooperative Agreements	66.811	150,463
U.S.-Mexico Border Grants Program	66.930	150,000
Other-U.S. Environmental Protection Agency	66.999	<u>8,376</u>
<b>Total Excluding Clusters</b>		<b>1,383,841,134</b>
<b>Research and Development Cluster</b>		
Wetlands Protection-State and Tribal Development Grants	66.461	82,201
Consolidated Pesticide Enforcement Cooperative Agreements	66.700	33,557
Pollution Prevention Grants Program	66.708	97,904
Other-U.S. Environmental Protection Agency	66.999	<u>46,815</u>
<b>Total Research and Development Cluster</b>		<b><u>260,477</u></b>
<b>Total U.S. Environmental Protection Agency</b>		<b><u>1,384,101,611</u></b>
<b>Department of Energy</b>		
State Energy Conservation	81.041	3,422,006
Weatherization Assistance for Low-Income Persons	81.042	3,081,444
Conservation Research and Development	81.086	12,588
Environmental Restoration	81.092	657,595
National Industrial Competitiveness through Energy, Environment, and Economics	81.105	<u>849,759</u>
<b>Total Department of Energy</b>		<b><u>8,023,392</u></b>
<b>Federal Emergency Management Agency</b>		
Hazardous Materials Training Program for Implementation of the Superfund Amendment and Reauthorization Act of 1986	83.011	163,367
State Disaster Preparedness Grants	83.505	160,979
Earthquake Hazards Reduction Grants	83.521	186,858
Emergency Management-State and Local Assistance	83.534	677,311
Mitigation Assistance	83.535	52,863
Flood Mitigation Assistance	83.536	162,079
Individual and Family Grants	83.543	311,000
Public Assistance Grants	83.544	399,222,804
Hazard Mitigation Grant	83.548	115,373,221
Project Impact: Building Disaster Resistant Communities	83.551	3,182

Federal Agency/Program Title	Federal Catalog Number	Grant Amount Received
Emergency Management Performance Grants	83.552	10,126,229
Other - Federal Emergency Management Agency	83.999	<u>450,230</u>
<b>Total Excluding Clusters</b>		526,890,123
<b>Research and Development Cluster</b>		
Earthquake Hazards Reduction Grants	83.521	58,809
Emergency Management Performance Grants	83.552	600,600
Other - Federal Emergency Management Agency	83.999	<u>309,000</u>
<b>Total Research and Development Cluster</b>		<u>968,409</u>
<b>Total Federal Emergency Management Agency</b>		<u>527,858,532</u>
<b>Department of Education</b>		
Adult Education-State Grant Program	84.002	39,776,161
Title I Grants to Local Educational Agencies	84.010	972,974,068
Migrant Education-Basic State Grant Program	84.011	106,801,142
Title I Program for Neglected and Delinquent Children	84.013	3,527,848
Services for Children with Deaf-Blindness	84.025	307
Special Education-Personnel Development and Parent Training	84.029	198
Vocational Education-Basic Grants to States	84.048	106,513,332
Vocational Education-State Councils	84.053	302,956
Leveraging Educational Assistance Partnership	84.069	6,452,451
Rehabilitation Services - Vocational Rehabilitation Grants to States	84.126	237,921,553
Rehabilitation Services-Service Projects	84.128	929,775
Public Library Construction and Technology Enhancement	84.154	808,389
Immigrant Education	84.162	33,292,857
Independent Living-State Grants	84.169	1,869,076
Rehabilitation Services-Independent Living Services for Older Individual Who are Blind	84.177	344,507
Special Education-Grants for Infants and Families with Disabilities	84.181	58,758,435
Byrd Honors Scholarships	84.185	8,698,625
Safe and Drug-Free Schools-State Grants	84.186	52,894,718
Supported Employment Services for Individuals with Severe Disabilities	84.187	2,353,334
Bilingual Education Support Services	84.194	1,298,188
Bilingual Education - Professional Development	84.195	141,000
Education for Homeless Children and Youth	84.196	2,834,011
Even Start-State Educational Agencies	84.213	14,689,221
Fund for the Improvement of Education	84.215	435,319
Capital Expenses	84.216	2,196,598
Assistive Technology	84.224	1,343,545

Federal Agency/Program Title	Federal Catalog Number	Grant Amount Received
Tech-Prep Education	84.243	9,239,087
Rehabilitation Training-State Vocational Rehabilitation Unit In-Service Training	84.265	383,004
Goals 2000-State and Local Education Systematic Improvement Grants	84.276	36,759,369
School to Work Opportunities	84.278	32,559,644
Eisenhower Professional Development State Grants	84.281	36,969,670
Charter Schools	84.282	13,326,648
Innovative Education Program Strategies	84.298	43,747,551
Even Start-Statewide Family Literacy Program	84.314	23,886
Technology Literacy Challenge Fund Grants	84.318	37,259,725
Special Education-State Program Improvement Grants for Children with Disabilities	84.323	1,564,259
Advanced Placement Incentive Program	84.330	375,959
Grants to States for Incarcerated Youth Offenders	84.331	1,170,379
Comprehensive School Reform Demonstration	84.332	15,385,842
Teacher Quality Enhancement Grants	84.336	1,002,859
Class Size Reduction	84.340	134,121,387
Preparing Tomorrow's Teachers to Use Technology	84.342	270,441
Title I Accountability Grants	84.348	<u>16,324,061</u>
<b>Total Excluding Clusters</b>		2,037,641,385
<b>Student Financial Aid Cluster</b>		
Federal Family Education Loans	84.032	16,599,808,011 ***
<b>Special Education Cluster</b>		
Special Education-Grants to States	84.027	498,925,541
Special Education-Preschool Grants	84.173	<u>23,266,370</u>
<b>Total Special Education Cluster</b>		<u>522,191,911</u>
<b>Total U.S. Department of Education</b>		<u>19,159,641,307</u>
<b>Consumer Product Safety Commission</b>		
Other-Consumer Product Safety Commission	87.999	56,623
<b>Department of Health and Human Services</b>		
Public Health and Social Services Emergency Fund	93.003	32,212
Special Programs for the Aging-Title VII, Chapter 3-Programs for Prevention of Elder Abuse, Neglect, and Exploitation	93.041	458,113
Special Programs for the Aging-Title VII, Chapter 2 - Long Term Care Ombudsman Services for Older Individuals	93.042	839,296

Federal Agency/Program Title	Federal Catalog Number	Grant Amount Received
Special Programs for the Aging-Title III, Part F-Disease Prevention and Health Promotion Services	93.043	1,720,745
Special Programs for the Aging-Title III, Part D-In-Home Services for Frail Older Individuals	93.046	12
Special Programs for the Aging-Title IV, Training, Research and Discretionary Projects and Programs	93.048	179,853
Grants for Residential Treatment Programs for Pregnant and Postpartum Women	93.101	724,557
Demonstration Grants for Residential Treatment for Women and Their Children	93.102	353,846
Food and Drug Administration-Research	93.103	2,045,584
Maternal and Child Health Federal Consolidated Programs	93.110	96,631
Project Grants and Cooperative Agreements for Tuberculosis Control Programs	93.116	7,489,560
Grants for Technical Assistance Activities Related to the Block Grant for Community Mental Health Services Technical Assistance Centers for Evaluation	93.119	42,520
Emergency Medical Services for Children	93.127	91,374
Primary Care Services - Resource Coordination and Development Primary Care Offices	93.130	402,650
Injury Prevention and Control Research and State and Community Based Programs	93.136	133,668
Projects for Assistance in Transition from Homelessness	93.150	3,841,410
Health Program for Toxic Substances and Disease Registry	93.161	948,164
Grants for State Loan Repayment	93.165	767,366
Cooperative Agreements for Drug Abuse Treatment Improvement Projects in Target Cities	93.196	1,323,493
Demonstration Cooperative Agreements for Development and Implementation of Criminal Justice Treatment Networks	93.229	685,852
Traumatic Brain Injury-State Demonstration Grant Program	93.234	32,251
Cooperative Agreements for State Treatment Outcomes and Performance Pilot Studies Enhancement	93.238	532,553
Childhood Immunization Grants	93.268	147,192,772 *
Centers for Disease Control and Prevention-Investigations and Technical Assistance	93.283	2,783,201
Promoting Safe and Stable Families	93.556	32,982,224
Temporary Assistance for Needy Families	93.558	4,204,719,293
Family Support Payments to States-Assistance Payments	93.560	26,400
Child Support Enforcement	93.563	118,224,158
Refugee and Entrant Assistance-State Administered Programs	93.566	33,338,873
Low-Income Home Energy Assistance	93.568	85,752,839
Community Services Block Grant	93.569	52,220,720
Community Services Block Grant - Discretionary Award	93.570	44,462
Community Services Block Grant Discretionary Awards-Community Food and Nutrition	93.571	454,498

Federal Agency/Program Title	Federal Catalog Number	Grant Amount Received
Refugee and Entrant Assistance-Discretionary Grants	93.576	5,633,900
Repatriation Program	93.579	14,193
Refugee and Entrant Assistance-Targeted Assistance	93.584	7,850,656
Empowerment Zones Program	93.585	3,586,422
Community-Based Family Resource and Support Grants	93.590	3,184,160
Welfare Report Research, Evaluations and National Studies	93.595	102,191
Grants to States for Access and Visitation Programs	93.597	876,151
Head Start	93.600	171,963
Child Support Enforcement Demonstrations and Special Projects	93.601	61,200
Adoption Incentive Payments	93.603	1,870,547
Developmental Disabilities Basic Support and Advocacy Grants	93.630	4,613,839
Children's Justice Grants to States	93.643	832,617
Child Welfare Services-State Grants	93.645	33,917,703
Adoption Opportunities	93.652	249,054
Foster Care-Title IV-E	93.658	1,192,113,549
Adoption Assistance	93.659	175,468,738
Social Services Block Grant	93.667	218,686,277
Child Abuse and Neglect State Grants	93.669	4,487,247
Family Violence Prevention and Services/Grants for Battered Women's Shelters_Grants to States and Indian Tribes	93.671	9,055,319
Independent Living	93.674	21,523,444
State Children's Insurance Program	93.767	259,842,527
Medicare-Supplementary Medical Insurance	93.774	8,443,303
Health Care Financing and Research, Demonstrations and Evaluations	93.779	1,045,022
Model Comprehensive Drug Abuse Treatment Programs for Critical Populations	93.902	501
Grants to States for Operation of Offices of Rural Health	93.913	288,908
HIV Care Formula Grants	93.917	110,713,389
Cooperative Agreements for State-Based Comprehensive Breast and Cervical Cancer Early Detection Program	93.919	4,884,472
Cooperative Agreements to Support Comprehensive School Health Programs to Prevent the Spread of HIV and Other Important Health Problems	93.938	1,003,071
HIV Prevention Activities: Health Department Based	93.940	10,643,394
HIV Demonstration, Research, Public and Professional Education Projects	93.941	206,289
Epidemiologic Research Studies of Acquired Immunodeficiency Syndrome (AIDS) and Human Immunodeficiency Virus (HIV) Infection in Selected Population Groups	93.943	494,057
Human Immunodeficiency Virus (HIV)/Acquired Immunodeficiency Virus Syndrome (AIDS) Surveillance	93.944	1,451,551
Assistance Program for Chronic Disease Prevention and Control	93.945	335,893



Federal Agency/Program Title	Federal Catalog Number	Grant Amount Received
Demonstration Grants to States with Respect to Alzheimer's Disease	93.951	185,263
Block Grants for Community Mental Health Services	93.958	43,599,612
Block Grants for Prevention and Treatment of Substance Abuse	93.959	259,995,321
Preventive Health Services-Sexually Transmitted Disease Control Grants	93.977	3,528,832
Preventive Health Services- Sexually Transmitted Diseases Research, Demonstrations, and Public Information and Education Grants	93.978	866,603
Mental Health Disaster Assistance and Emergency Mental Health Health Program for Refugees	93.982	71,181
	93.987	926,987
Cooperative Agreements for State-Based Diabetes Control Program and Evaluation of Surveillance Systems	93.988	243,903
Preventive Health and Health Services Block Grant	93.991	15,289,484
Maternal and Child Health Services Block Grant to the States	93.994	35,251,306
Other-Department of Health and Human Services	93.999	<u>12,757,353</u>
<b>Total Excluding Clusters</b>		7,156,848,542
<b>Aging Cluster</b>		
Special Programs for the Aging-Title III, Part B-Grants for Supportive Services and Senior Centers	93.044	28,847,989
Special Programs for the Aging-Title III, Part C-Nutrition Services	93.045	<u>46,978,002</u>
<b>Total Aging Cluster</b>		75,825,991
<b>Child Care Cluster:</b>		
Child Care and Development Block Grant	93.575	462,628,427
Child Care Mandatory and Matching Funds of the Child Care and Development Fund	93.596	<u>269,048,961</u>
<b>Total Child Care Cluster</b>		731,677,388
<b>Medicaid Cluster</b>		
State Medicaid Fraud Control Units	93.775	10,593,241
State Survey and Certification of Health Care Providers and Suppliers	93.777	23,103,580
Medical Assistance Program	93.778	<u>13,261,920,047</u>
<b>Total Medicaid Cluster</b>		<u>13,295,616,868</u>
<b>Total U.S. Department of Health and Human Services</b>		<u>21,259,968,789</u>
<b>Corporation for National and Community Service</b>		
State Commission(s)	94.003	1,334,743
Learn and Serve America-School and Community Based Programs	94.004	2,692,390
AmeriCorps	94.006	<u>24,219,295</u>
<b>Total Excluding Clusters</b>		28,246,428

Federal Agency/Program Title	Federal Catalog Number	Grant Amount Received
<b>Foster Grandparent/Senior Companion Cluster:</b>		
Foster Grandparent Program	94.011	<u>1,412,387</u>
<b>Total Corp. for National and Community Service</b>		<u>29,658,815</u>
 <b>Social Security Administration</b>		
<b>Disability Insurance/SSI Cluster</b>		
Social Security-Disability Insurance	96.001	173,403,979
 <b>Office Of National Drug Control Policy</b>		
High Intensity Drug Trafficking Area	See Note 4	3,745,885
 <b>Miscellaneous Grants and Contracts</b>		
Shared Revenue-Flood Control Lands	98.002	332,907
Shared Revenue-Grazing Land	98.004	173,469
Capital Outlay - Reed Act	98.012	33,974,195
U.S. Department of the Interior-Fire Prevention/Suppression Agreement	98.014	134,000
U.S. Department of the Interior-Fire Prevention/Suppression Agreement	98.015	160,367
U.S. Department of Agriculture and Various Other U.S. Department-Fire Prevention/Suppression	98.016	54,631,667
Miscellaneous Federal Receipts	98.099	504,774
Miscellaneous Federal Receipts	98.999	<u>2,599,388</u>
<b>Total Miscellaneous</b>		<u>92,510,767</u>
<b>Total Federal Awards Received</b>		<b><u>\$52,884,091,328</u></b>

\* Amount includes value of commodities or food stamps.

\*\* Amount includes donated property.

\*\*\* Amount includes loans and insurance in effect as of June 30, 2001.

**NOTES TO THE SCHEDULE OF FEDERAL ASSISTANCE  
FISCAL YEAR ENDED JUNE 30, 2001**

**1. General**

The accompanying State of California Schedule of Federal Assistance presents the total amount of federal financial assistance programs received by the State of California for the fiscal year ended June 30, 2001. This schedule does not include expenditures of federal grants received by the University of California, the California State University, and the California Housing Finance Agency. The expenditures of the University of California, California State University, and California Housing Finance Agency are audited by other independent auditors in accordance with the U.S. Office of Management and Budget, Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations* (OMB Circular A-133).

The \$52,884,091,328 in total federal assistance consists of the following:

Cash assistance received	\$33,193,062,517
Noncash federal awards	1,849,483,576
Loans and/or loan guarantees outstanding	14,951,010,229
Insurance in-force	<u>2,890,535,006</u>
<b>Total</b>	<b>\$52,884,091,328</b>

**2. Basis of Accounting**

OMB Circular A-133 and the Single Audit Act of 1984 (Amended 1996) require the Schedule of Federal Assistance to present total expenditures for each federal assistance program. However, although the state accounting system separately identifies revenues for each federal assistance program, it does not separately identify expenditures for each program. As a result, the State prepares its Schedule of Federal Assistance on a cash receipts basis. The schedule shows the amount of cash and noncash federal assistance received, loans and loan guarantees outstanding, and insurance in force for the year ended June 30, 2001.

**3. Unemployment Insurance**

Of the \$2,980,142,166 in total unemployment insurance funds (federal catalog number 17.225) received by the Employment Development Department during fiscal year 2000-01, \$2,662,047,204 was State Unemployment Insurance funds that were drawn down from the Unemployment Trust Fund in the U.S. Treasury.

#### 4. Other

The California Department of Justice (DOJ) receives cash reimbursements from local law enforcement agencies under the Office of National Drug Control Policy's High Intensity Drug Trafficking Area program. During the period July 1, 2000 through June 30, 2001, the DOJ received the following cash reimbursements from pass-through entities:

Federal Agency/Program	Pass-through Entity	Grant Number	Amount	
Office of National Drug Control Policy/ High Intensity Drug Trafficking Area	City of San Diego	18PSCP575	\$ 65,482	
		19PSCP575	523,575	
		10PSCP575	1,618,779	
		11PSCP575	342,345	
	City of Hawthorne	18PLAP534	72,997	
		19PLAP534	68,698	
		10PLAP534	905,808	
		18PLAP541	481	
		19PLAP541	100,146	
		10PLAP541	47,574	
			Total	<u>\$3,745,885</u>

The State was also loaned Federal Excess Personal Property (FEPP) from the U.S. Forest Service during the period July 1, 2000 to June 30, 2001. According to the California Department of Forestry and Fire Protection, the amount loaned from July 1, 2000 to June 30, 2001, was \$3,045,725. The U.S. Forest Service and the State maintain the FEPP program at federal acquisition costs of the property.

## **Summary Schedule of Prior Audit Findings**

**Prepared by  
Department of Finance**

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## **SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS**

Reference Number: **2000-12-1**

Federal Catalog Number: All Programs

State Administering Department: Department of Finance

Fiscal Year Finding Initially Reported: 1995-96

Audit Finding: Reporting Requirements. Because of limitations in its automated accounting systems, the State has not complied with the provision of OMB Circular A-133 requiring a schedule showing total expenditures for each federal program.

Status of Corrective Action: Uncorrected. The State's accounting system will require substantial modification to meet all federal and state requirements. The State will address changes in relation to other priorities and costs.<sup>1</sup>

Reference Number: **2000-3-7**

Federal Catalog Number: 10.558

State Administering Department: Department of Education

Fiscal Year Finding Initially Reported: 1998-99

Audit Finding: Cash Management. The Department of Education does not have adequate procedures for recovering cash advances in a timely manner from food program participants who are no longer entitled to these funds.

Status of Corrective Action: Fully corrected.

Reference Number: **2000-5-3**

Federal Catalog Number: 10.558

State Administering Department: Department of Education

Fiscal Year Finding Initially Reported: 1996-97

Audit Finding: Eligibility. The Department of Education needs to improve its process for ensuring that certain institutions participating in the food program meet the applicable licensing or approval requirements.

Status of Corrective Action: Fully corrected.

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Endnotes begin on page 167.

Reference Number: **2000-7-2**  
Federal Catalog Number: 10.555  
State Administering Department: Department of Education  
Fiscal Year Finding Initially Reported: 1998-99  
Audit Finding: Matching, Reporting. The Department of Education lacked adequate controls and documentation to support its reported state match.  
Status of Corrective Action: Fully corrected.

Reference Number: **2000-14-5**  
Federal Catalog Number: 10.550  
State Administering Department: Department of Education  
Fiscal Year Finding Initially Reported: 1998-99  
Audit Finding: Special Tests and Provisions. The Department of Education (CDE) did not properly account for its donated foods.  
Status of Corrective Action: Partially corrected. Anticipated correction date is December 31, 2001. CDE continues to closely monitor the monthly inventory reconciliation process at the Sacramento warehouse.

Reference Number: **2000-3-5**  
Federal Catalog Number: 10.557, 93.268  
State Administering Department: Department of Health Services  
Fiscal Year Finding Initially Reported: 1999-00  
Audit Finding: Cash Management. The Department of Health Services did not minimize the time between the receipt and disbursement of federal program funds for two programs reviewed.  
Status of Corrective Action: Fully corrected.



Reference Number: **2000-13-1**

Federal Catalog Number: 10.557, 93.917, 93.994

State Administering Department: Department of Health Services

Fiscal Year Finding Initially Reported: 1998-99

Audit Finding: Subrecipient Monitoring. The Department of Health Services (DHS) lacks an adequate system to ensure it promptly receives all audit reports from nonprofit subrecipients required to submit one and issues management decisions on reported findings.

Status of Corrective Action:

- a. HIV Care Formula Grants: Fully corrected.
- b. Maternal and Child Health Services Block Grant: Partially corrected. DHS is implementing a system to identify and track non-profit subrecipients who are subject to OMB Circular A-133 audits. This system involves the development of a protocol for promptly issuing management decisions on audit findings. This protocol has been developed by the California Women, Infants, and Children (WIC) Branch, in conjunction with other DHS programs. Moreover, this protocol is based upon expert advice from the DHS Audits and Investigations (A&I) Division, as well as the WIC Branch and other Primary Care and Family Health programs. In the majority of cases, the Maternal and Child Health Branch issues the management decision. In those cases where a subrecipient is out of compliance with OMB Circular A-133, A&I has agreed to provide fiscal technical assistance to the subrecipient and to issue the management decision when the issue is resolved.

In addition, this system includes revising current contract language. The language will be revised to state that a separate letter must be attached to the audit for those contractors that submit an audit other than an OMB A-133 audit. This letter must be signed and certified by the contractor stating that, under penalty of perjury, the contractor has not expended \$300,000 or more in federal funds for the year in question. Affected DHS programs have agreed to meet on a quarterly basis until this system is fully operational.<sup>2</sup>

Reference Number: **2000-13-2**

Federal Catalog Number: 10.550, 10.553, 10.555, 10.556, 10.558, 10.559, 84.002, 93.575, and 93.596

State Administering Department: Department of Education

Fiscal Year Finding Initially Reported: 1996-97

Audit Finding: Subrecipient Monitoring. The Department of Education did not sufficiently monitor the audit reports of its nonprofit subrecipients.

Status of Corrective Action: Fully corrected.

Reference Number: **2000-2-2**

Federal Catalog Number: 17.207, 17.225, 17.250, 17.801, 17.804, 17.253, and 84.278

State Administering Department: Employment Development Department

Fiscal Year Finding Initially Reported: 1998-99

Audit Finding: Allowable Costs and Cost Principles. The Employment Development Department lacked documentation supporting some of its payroll and operating costs allocated to federal programs.

Status of Corrective Action: Fully corrected.<sup>3</sup>

Reference Number: **2000-9-4**

Federal Catalog Number: 83.544, 83.548

State Administering Department: Office of Emergency Services

Fiscal Year Finding Initially Reported: 1999-00

Audit Finding: Suspension and Debarment. The Office of Emergency Services (OES) did not require Public Assistance Grants and Hazard Mitigation Grant program applicants to submit suspension and debarment certifications.

Status of Corrective Action: Finding remains uncorrected. The OES disagrees with this finding. The Bureau of State Audits (BSA) reports that it "...contacted the Federal Emergency Management Agency (FEMA) legal staff for an interpretation of how this regulation applies. The FEMA legal staff indicated that suspension and disbarment requirements do not apply to the initial response to a disaster, but would apply to the later recovery operations." OES maintains that this undocumented opinion is inconsistent with 44 Code of Federal Regulations (CFR) 17.110(a) (2) (v), which clearly

intends to encompass both the initial response period and recovery period, in that it references both emergencies and disasters. Furthermore, 44 CFR 17.110(a)(2)(v) offers no guidance concerning when “initial response” activities end, and “later recovery transactions” begin. OES also notes that FEMA program staff continues to maintain that FEMA grants are exempt under this regulation, and they do not require OES, as grantee, to take any special actions with regards to suspended and debarred contractors. Therefore, OES does not agree with the BSA interpretation and does not expect to change its grant requirements until FEMA changes the regulations, or issues a nationally recognized policy establishing the demarcation between “initial response” and “later recovery transactions.” OES further advises the BSA that the Public Assistance and Hazard Mitigation programs recently underwent a management audit by the FEMA Inspector General, and there was no mention of any deficiency in this area.<sup>4</sup>

Reference Number: **2000-12-4**

Federal Catalog Number: 85.544, 83.548

State Administering Department: Office of Emergency Services

Fiscal Year Finding Initially Reported: 1999-00

Audit Finding: Reporting. The Office of Emergency Services' (OES) financial status reports contain unsupported expenditure information. As a result, FEMA cannot rely on these reports to accurately assess program status.

Status of Corrective Action: Finding remains uncorrected. OES continues to experience staffing shortages as well as limited functions with the accounting system OES is mandated to utilize for our daily transactions. Further, due to the age of many of the federal grants (6 to 12 years), many records are not available or incomplete for all parties including the recipients. Therefore, we continue to negotiate with FEMA on an on-going basis regarding the appropriate reporting of grant expenditures, administrative allowances and other pertinent information.<sup>5</sup>

Reference Number: **2000-12-5**

Federal Catalog Number: 83.544 and 83.548

State Administering Department: Office of Emergency Services

Fiscal Year Finding Initially Reported: 1997-98

Audit Finding: Reporting. In fiscal year 1999-00, the Office of Emergency Services (OES) did not reconcile the receipts

and disbursements reported in its federal cash transaction reports to its official accounting records.

Status of Corrective Action: Finding remains uncorrected. OES has not been successful in obtaining approval for additional staff that would be necessary to develop procedures and perform the more detailed reconciliation in addition to many other functions. OES does perform a general monthly reconciliation for receipts and disbursements that encompasses all accounting transactions for the Federal Trust Fund. It is OES's intention to make another attempt to request additional positions in the next Budget Year.<sup>6</sup>

Reference Number: **2000-13-7**

Federal Catalog Number: 83.544 and 83.548

State Administering Department: Office of Emergency Services

Fiscal Year Finding Initially Reported: 1996-97

Audit Finding: Subrecipient Monitoring. The Office of Emergency Services does not ensure that a management decision regarding the resolution of audit findings is made within six months after it receives an audit report.

Status of Corrective Action: Fully corrected.<sup>7</sup>

Reference Number: **2000-1-1**

Federal Catalog Number: 84.181

State Administering Department: Department of Developmental Services

Fiscal Year Finding Initially Reported: 1998-99

Audit Finding: Activities Allowed. The Department of Developmental Services has not developed and implemented sufficient procedures to ensure that it disburses Early Intervention funds for allowable purposes.

Status of Corrective Action: Fully corrected.

Reference Number: **2000-1-2**

Federal Catalog Number: 84.181

State Administering Department: Department of Education

Fiscal Year Finding Initially Reported: 1999-00

Audit Finding: Activities Allowed. The Department of Education (CDE) did not ensure that it disbursed Early Intervention program funds for allowable purposes, when it paid several subrecipients 75 percent of their individual grant awards without receiving and approving their applications.

Status of Corrective Action: Partially corrected. Anticipated correction date is December 31, 2001. To ensure that program applications are approved prior to disbursement of program funds, CDE has transferred responsibility for the Early Intervention program to the Administrative Services Unit within the Special Education Division. CDE will not disburse 2001-02 program funds without the proper review and approval of applications.

Reference Number: **2000-1-3**

Federal Catalog Number: 84.027 and 84.173

State Administering Department: Department of Education

Fiscal Year Finding Initially Reported: 1999-00

Audit Finding: Activities Allowed. The Department of Education did not ensure that it disbursed Special Education—Grants to States and Special Education—Preschool Grants program funds for allowable purposes.

Status of Corrective Action: Fully corrected.

Reference Number: **2000-2-3**

Federal Catalog Number: 84.011

State Administering Department: Department of Education

Fiscal Year Finding Initially Reported: 1999-00

Audit Finding: Allowable Costs and Cost Principles. The Department of Education approved the use of \$66,000 in Migrant Education funds without determining whether they are reasonable as required by OMB Circular A-87.

Status of Corrective Action: Fully corrected.<sup>8</sup>

Reference Number: **2000-2-4**

Federal Catalog Number: 84.011

State Administering Department: Department of Education

Fiscal Year Finding Initially Reported: 1999-00

Audit Finding: Allowable Costs and Cost Principles. The Department of Education (CDE) approved the use of \$37,900 in Migrant Education funds during fiscal year 1999-00 that may not be an efficient use of resources as required by OMB Circular A-87.

Status of Corrective Action: Finding remains uncorrected. CDE continues to seek approval of its sole source contract with Tromik Technology Corporation for technical services relating to the reporting of migrant pupil data and a Feasibility Study Report for the Migrant Education Program Student Information System.<sup>9</sup>

Reference Number: **2000-3-1**

Federal Catalog Number: 84.048

State Administering Department: California Community Colleges, Chancellor's Office

Fiscal Year Finding Initially Reported: 1997-98

Audit Finding: Cash Management, Subrecipient Monitoring. The California Community Colleges, Chancellor's Office lacks adequate procedures to ensure subrecipients of the Vocational Education program minimize the time elapsing between the receipt and use of federal program funds. Additionally, it does not sufficiently monitor these subrecipients' use of the funds.

Status of Corrective Action: Fully corrected.<sup>10</sup>

Reference Number: **2000-3-2**

Federal Catalog Number: 84.243

State Administering Department: California Community Colleges, Chancellor's Office

Fiscal Year Finding Initially Reported: 1997-98

Audit Finding: Cash Management. The California Community Colleges, Chancellor's Office lacks adequate procedures to ensure subrecipients of the Tech-Prep program minimize the time elapsing between the receipt and use of federal program funds.

Status of Corrective Action: Fully corrected.<sup>10</sup>

Reference Number: **2000-3-3**

Federal Catalog Number: 84.186

State Administering Department: Department of Alcohol and Drug Programs

Fiscal Year Finding Initially Reported: 1999-00

Audit Finding: Cash Management, Subrecipient Monitoring. The Department of Alcohol and Drug Programs (DADP) lacks adequate procedures to ensure subrecipients of the Safe and Drug-Free Schools and Communities—State Grants program minimize the time elapsing between receipt and use of program funds. In addition, it does not sufficiently monitor the subrecipients' use of the funds.

Status of Corrective Action:

- a. Cash Management: Partially corrected. Anticipated correction date is July 1, 2002. Counties are required to submit Quarterly Federal Financial Management Reports (QFFMR). A series of up to three letters may be sent if a county does not submit its QFFMR. Payments to counties have not been adjusted to reflect actual expenditure patterns. Adjustments to county payments will be made no later than the first payment commencing after July 1, 2002, as this is the first year of major changes to our allocation, contracting and payment system as well as revised quarterly reporting procedures.<sup>11</sup>
- b. Subrecipient Monitoring: Uncorrected. The DADP disagrees with this portion of the finding. DADP will resolve the matter with the U.S. Department of Education (DOE). The audit finding cites the DADP for not performing site visits to monitor the counties. While the DADP agrees that it is required to monitor subgrantees, per Public Law 104-156, there are other monitoring options in lieu of site visits. Such options include limited scope audits, or other means. In resolving the issue with the DOE, the DADP would like to discuss these options as well as the frequency and scope of any site visits that the DOE may require.

Reference Number: **2000-3-4**

Federal Catalog Number: 84.011

State Administering Department: Department of Education

Fiscal Year Finding Initially Reported: 1999-00

Audit Finding: Cash Management and Subrecipient Monitoring. The Department of Education (CDE) lacks adequate procedures to ensure that Migrant Education program subrecipients minimize the time elapsing between the

receipt and use of federal program funds. Additionally, it does not sufficiently monitor these subrecipients' use of the funds.

Status of Corrective Action: Partially corrected. Anticipated correction date is October 31, 2002. CDE expects to complete its review of its Migrant Education allocation procedures by June 30, 2002, for implementation in fiscal year 2002-03. CDE will begin its monitoring reviews of Migrant Education regions in October 2002.<sup>12</sup>

Reference Number: **2000-5-1**

Federal Catalog Number: 84.126

State Administering Department: Department of Rehabilitation

Fiscal Year Finding Initially Reported: 1996-97

Audit Finding: Eligibility. The Department of Rehabilitation (Rehabilitation) does not always determine applicant eligibility within the required time period and did not document how it determined eligibility for one of the applicants the Bureau of State Audits reviewed.

Status of Corrective Action: Partially corrected. Anticipated correction date is July 2002. Rehabilitation generally agrees with this finding. Rehabilitation is considering the Bureau's recommendation as part of its continuing efforts to streamline and improve the vocational rehabilitation process. The redesign and improvement of the vocational rehabilitation process is significant and complex. A major goal in the redesign and improvement of the vocational rehabilitation process is to provide counselors with more time to work closely with their consumers to provide quality vocational rehabilitation, and, consequently, be enabled to make more effective and timely decisions in the determination of eligibility.

Rehabilitation will be holding a statewide District Administrators' meeting in November 2001 and will be discussing this finding. Rehabilitation is committed to identify "best practices" in the determination of eligibility for consumers. Through preliminary analysis of the causes for the finding, Rehabilitation has identified districts that are managing the eligibility determination process most effectively. Those districts' management practices will be shared with all of the districts.

In addition, based upon recommendations received from our Continuous Improvement Workgroup, Rehabilitation will provide counselors with focused training on eligibility determination. Rehabilitation will change its emphasis on eligibility determination as a compliance issue, and focus on eligibility determination as a customer service issue.



Rehabilitation anticipates the training effort can be completed by July 2002.<sup>13</sup>

Reference Number: **2000-8-1**  
Federal Catalog Number: 84.181  
State Administering Department: Department of Developmental Services  
Fiscal Year Finding Initially Reported: 1999-00  
Audit Finding: Period of Availability. The Department of Developmental Services inappropriately charged costs against an Early Intervention award for obligations that occurred before the award was available for expenditure.  
Status of Corrective Action: Fully corrected.

Reference Number: **2000-9-1**  
Federal Catalog Number: 84.181  
State Administering Department: Department of Education  
Fiscal Year Finding Initially Reported: 1999-00  
Audit Finding: Suspension and Debarment. The Department of Education did not always have signed suspension and debarment certifications for participants of the Early Intervention program.  
Status of Corrective Action: Fully corrected.

Reference Number: **2000-9-2**  
Federal Catalog Number: 84.243  
State Administering Department: California Community Colleges, Chancellor's Office.  
Fiscal Year Finding Initially Reported: 1997-98  
Audit Finding: Suspension and Debarment. The California Community Colleges, Chancellor's Office did not receive the required suspension and debarment certifications from all participants in the Tech-Prep program.  
Status of Corrective Action: Fully corrected.

Reference Number: **2000-12-2**  
Federal Catalog Number: 84.278

State Administering Department: Employment Development Department

Fiscal Year Finding Initially Reported: 1999-00

Audit Finding: Reporting. The Employment Development Department's (EDD) June 30, 2000, quarterly financial status report submitted to the U.S. Department of Education was incomplete.

Status of Corrective Action: Partially corrected. The EDD School-to-Career (STC) Office has implemented a system to improve reporting performance. Advance notification to the subgrantees combined with an automated tracking system has improved reporting performance, but has not totally eliminated late subgrantee expenditure reporting. However, aggressive follow-up on late reports has improved the submission rate and accuracy of reported financial expenditures. The STC has emphasized to all subgrantees the importance of submitting quarterly reports by the established deadline and stressed the consequences of late and inaccurate reporting.

The improved coordination between the STC office and the Fiscal Programs Division continues to improve the timeliness and completeness of expenditure data reported to the U.S. Department of Education. Significant progress has been achieved and continued emphasis will alleviate the problem of understated program expenditures.

Reference Number: **2000-12-3**

Federal Catalog Number: 84.186

State Administering Department: Department of Alcohol and Drug Programs

Fiscal Year Finding Initially Reported: 1999-00

Audit Finding: Period Availability, Reporting. The Department of Alcohol and Drug Programs spent \$2,562,167 of Safe and Drug-Free Schools and Communities State Grants program funds after the periods of availability for three of its grants ended. Additionally, it does not have adequate controls to ensure that its requests for federal funds agree with the grant expenditures for the program.

Status of Corrective Action: Fully corrected.<sup>14</sup>

Reference Number: **2000-13-3**

Federal Catalog Number: 84.340

State Administering Department: Department of Education

Fiscal Year Finding Initially Reported: 1999-00

Audit Finding: Subrecipient Monitoring. The Department of Education does not adequately monitor either its subrecipients' use of Class Size Reduction program funds or their activities.

Status of Corrective Action: Fully corrected.

Reference Number: **2000-13-4**

Federal Catalog Number: 84.027 and 84.173

State Administering Department: Department of Education

Fiscal Year Finding Initially Reported: 1998-99

Audit Finding: Subrecipient Monitoring. The Department of Education has not fully implemented a subrecipient monitoring system necessary to ensure that subrecipients of the Special Education—Grants to States program and Special Education—Preschool Grants program use federal grant money only for authorized purposes and take appropriate and timely corrective action on any deficiencies found.

Status of Corrective Action: Fully corrected.

Reference Number: **2000-13-5**

Federal Catalog Number: 84.048, 84.243

State Administering Department: California Community Colleges, Chancellor's Office

Fiscal Year Finding Initially Reported: 1995-96

Audit Finding: Subrecipient Monitoring. The California Community Colleges Chancellor's Office (Chancellor's Office) did not sufficiently monitor and follow up on the reported audit findings of the State's 71 community college districts for fiscal year 1998-99.

Status of Corrective Action: Partially corrected. Anticipated correction date is October 31, 2001. The Chancellor's Office process calls for a more timely review of the audit citations. We are currently in the process of issuing management decisions to the community college districts.

Reference Number: **2000-14-1**

Federal Catalog Number: 84.126

State Administering Department: Department of Rehabilitation

Fiscal Year Finding Initially Reported: 1999-00

Audit Finding: Special Tests and Provisions. The Department of Rehabilitation (Rehabilitation) did not always ensure that a maximum effort was made by the individual to secure grant assistance from other sources before training and training services were paid for with grant funds.

Status of Corrective Action: Partially corrected. Anticipated correction date is July 2002. The Comparable Benefits Workgroup was established in February 2001, and has been working to establish and implement a directive for all employees that clearly defines the policy and procedures necessary to ensure Rehabilitation's maximum efforts. The draft of the directive will be routed for review in October 2001.

The workgroup has also been working closely with the Collaborative Services Section to establish interagency agreements with the various education and financial aid agencies to ensure the consistent application of the regulations regarding vocational rehabilitation and financial aid opportunities for persons with disabilities. As part of this effort, the Comparable Benefits Workgroup will be recommending that counselors participate along with financial aid administrators in annual training that is provided by the Student Aid Commission (SAC). This training will provide information to the counselors regarding the requirements for applying for financial aid so that this information can be shared with consumers applying for grants and other financial aid.

The workgroup has also explored strategies to ensure documentation of the maximum efforts in the consumer's case file. The workgroup will be making a recommendation in this area as well. The workgroup will soon be presenting all of their final recommendations for management review and approval.

Regarding the one consumer who appeared to have received duplicate payment for education expenses, Rehabilitation later determined that the grant had been used for the consumer's living expenses in lieu of Rehabilitation providing maintenance expenses for this consumer. There was no duplicate payment to this consumer. The university received only one tuition payment and that was from Rehabilitation.

Reference Number: **2000-14-2**  
Federal Catalog Number: 84.010, 84.011  
State Administering Department: Department of Education  
Fiscal Year Finding Initially Reported: 1998-99

Audit Finding: Subrecipient Monitoring, Special Tests and Provisions. The Department of Education (CDE) did not sufficiently

monitor Local Educational Agencies to ensure they complied with the comparability requirement.

Status of Corrective Action: Finding remains uncorrected. CDE continues to work with the U.S. Department of Education to develop an effective monitoring process for the Title I and Migrant Education comparability requirement, which can be implemented using existing program resources. CDE expects to have a process in place by December 31, 2001.<sup>15</sup>

Reference Number: **2000-14-3**

Federal Catalog Number: 84.032

State Administering Department: California Student Aid Commission

Fiscal Year Finding Initially Reported: 1996-97

Audit Finding: Special Tests and Provisions. The California Student Aid Commission's (CSAC) auxiliary organization administers the loan program. The information the auxiliary organization reports to the federal government for computing the reinsurance rate is not always accurate; thus, the auxiliary organization may not be receiving the correct amount of funds.

Status of Corrective Action: Partially corrected. CSAC has an ongoing process to ensure loan and enrollment statuses are in agreement with all participating parties. CSAC and its auxiliary EDFUND recognize how important it is that CSAC/EDFUND loan records match the loan records of partnering lenders and schools. Over the last several years, major efforts have been undertaken and great strides have been made to insure that these separate databases are consistent and to minimize the instances where loan and enrollment statuses even could be inconsistent. It has been pointed out in prior responses to this issue that CSAC/EDFUND does not have control of the activities of schools, lenders, and the National Student Loan Data System (NSLDS) and their corresponding databases. This inherent lack of control means that some inconsistencies may (and in fact will) occur.

CSAC/EDFUND have continued to monitor the accuracy of the enrollment status by comparing the NSLDS enrollment data with its own records. Borrower records, if warranted, are corrected as a result of this status checking. Since the most recent single state audit was completed an additional process has been instituted whereby the total loan database is sampled and borrower statuses are verified against the NSLDS database. This process is now being performed regularly in order to identify and communicate with schools that do not promptly report status changes.

Reference Number: **2000-13-6**

Federal Catalog Number: 84.181 and 93.778

State Administering Department: Department of Developmental Services

Fiscal Year Finding Initially Reported: 1999-00

Audit Finding: Subrecipient Monitoring. The Department of Developmental Services (DDS) does not fulfill all of its subrecipient monitoring responsibilities.

Status of Corrective Action: Partially corrected. Anticipated Correction date is November 2001. During February 2000, the Bureau of State Audits (BSA) found that the DDS failed to provide subrecipients with information necessary to identify the federal sources of funds provided to them under the above-named grant. During March of 2001, DDS informed recipients of Early Intervention funds about the grant award numbers and names in order to correct the BSA's finding. The recipients include some regional centers as well as other organizations. They are informed about federal award names and numbers in an annual announcement. The subrecipients are informed during the process of completing an annual application for funding and the federal award number is contained on the final award contract.

DDS is also implementing procedures for informing all 21 regional centers of the federal award information for federal funding received from DDS. These procedures are expected to be in place by November 30, 2001.

Reference Number: **2000-2-1**

Federal Catalog Number: 93.778

State Administering Department: Department of Health Services

Fiscal Year Finding Initially Reported: 1999-00

Audit Finding: Allowable Costs and Cost Principles. The Department of Health Services (DHS) does not adequately use its automated claim payment system to prevent or minimize the overpayment of certain provider claims and did not adequately document denials of other health coverage.

Status of Corrective Action: a. Maximum Quantity of Prescription Drugs: Partially corrected. The Single Audit recommends DHS "enter in its system maximum 100-day supply for each prescription drug item." To accomplish this, DHS will need to change the "maximum quantity" data element for each drug listing in the Formulary File.

DHS recognized this issue prior to the Single Audit. Historically, DHS has issued instructions to Electronic Data Systems (EDS), the Medi-Cal fiscal intermediary, to change the maximum quantities of various drugs on a case-by-case basis. Because the case-by-case review and implementation of maximum quantities is a slow, laborious process for which neither DHS nor EDS have adequate pharmacist staffing, an alternative approach was necessary. Due to the need to be more efficient in altering maximum quantities, (the value used to establish the 100 day supply quantity limit) the DHS and EDS began a systematic approach to altering the maximum quantity. EDS proposed this systematic approach in Cost Containment Proposal (CCP) #98-008. Subsequently, DHS issued Operational Instruction Letter #333-99, December 14, 1999, directing EDS to implement the maximum quantity strategies outlined in CCP #98-008. Additionally, DHS and EDS are currently reviewing the maximum quantity of injectable drug products which tend to be a large percentage of the billing errors reviewed. This review will most likely result in a decrease in the maximum quantity allowed for various injectable drugs.

In addition to this systematic approach, DHS continues to review erroneous billed amounts through the drug rebate dispute resolution process. When it identifies an erroneous billing amount, DHS reviews the maximum quantity of the drug and implements changes as necessary to prevent future errors. The Rebate Accounting and Information System (RAIS) which is scheduled to be implemented January 1, 2002, will aid in this review. DHS is designing RAIS reports to help identify erroneous billing quantities as a tool in establishing future quantity edits. Based on these efforts, DHS believes it is complying with the BSA's recommendation; DHS' current efforts to revise maximum quantities will prevent a significant number of erroneous claims from being processed, therefore reducing overpayment of provider drug claims.

- b. Overpayment of Long Term Care Claims: Fully corrected.
- c. Retention of Medicare Denials: Fully corrected.

Reference Number: **2000-3-6**

Federal Catalog Number: 93.767

State Administering Department: Managed Risk Medical Insurance Board

Fiscal Year Finding Initially Reported: 1999-00

Audit Finding: Cash Management. The Managed Risk Medical Insurance Board did not adequately minimize the amount of time elapsing between the transfer of federal funds to the State and their disbursement for program costs.

Status of Corrective Action: Fully corrected.

Reference Number: **2000-5-2**

Federal Catalog Number: 93.767

State Administering Department: Managed Risk Medical Insurance Board

Fiscal Year Finding Initially Reported: 1999-00

Audit Finding: Eligibility. The Managed Risk Medical Insurance Board does not always ensure it enrolls into the program only eligible individuals.

Status of Corrective Action: Fully corrected.

Reference Number: **2000-7-1**

Federal Catalog Number: 93.994

State Administering Department: Department of Health Services

Fiscal Year Finding Initially Reported: 1999-00

Audit Finding: Earmarking. The Department of Health Services does not have adequate procedures to ensure that it meets the program's earmarking requirements.

Status of Corrective Action: Fully corrected.<sup>16</sup>

Reference Number: **2000-9-3**

Federal Catalog Number: 93.268, 93.917, and 93.994

State Administering Department: Department of Health Services

Fiscal Year Finding Initially Reported: 1998-99

Audit Finding: Suspension and Debarment. The Department of Health Services did not always require participants to submit signed suspension and debarment certifications.

Status of Corrective Action: Fully corrected.<sup>17</sup>

Reference Number: **2000-10-1**

Federal Catalog Number: 93.767



State Administering Department: Managed Risk Medical Insurance Board  
Fiscal Year Finding Initially Reported: 1998-99  
Audit Finding: Program Income. The Managed Risk Medical Insurance Board does not prepare an adequate reconciliation to ensure that it receives all program income it has earned.  
Status of Corrective Action: Fully corrected.

Reference Number: **2000-12-6**

Federal Catalog Number: 93.994

State Administering Department: Department of Health Services

Fiscal Year Finding Initially Reported: 1999-00

Audit Finding: Reporting. The Department of Health Services does not always report complete information in its annual program report to the U.S. Department of Health and Human Services.

Status of Corrective Action: Fully corrected.<sup>18</sup>

Reference Number: **2000-12-7**

Federal Catalog Number: 93.674

State Administering Department: Department of Social Services

Fiscal Year Finding Initially Reported: 1998-99

Audit Finding: Reporting. The Department of Social Services still does not ensure that counties expending Independent Living Program funds include all the required information on their performance reports.

Status of Corrective Action: Fully corrected.

Reference Number: **2000-14-4**

Federal Catalog Number: 93.268

State Administering Department: Department of Health Services

Fiscal Year Finding Initially Reported: 1999-00

Audit Finding: Special Tests and Provisions. The Department of Health Services did not properly account for its vaccine inventory when it reported incomplete inventory information to the

Centers for Disease Control and Prevention (federal agency).

Status of Corrective Action: Fully corrected.

Reference Number: **2000-14-6**

Federal Catalog Number: 93.778

State Administering Department: Department of Health Services

Fiscal Year Finding Initially Reported: 1997-98

Audit Finding: Special Tests and Provisions. The Department of Health Services does not have adequate controls over provider agreements and disclosures.

Status of Corrective Action: Fully corrected.<sup>19</sup>

## ENDNOTES—AUDITOR COMMENTS

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<sup>1</sup> The status of this issue remains unchanged. Please refer to reference number **2001-12-7** for additional information.

<sup>2</sup> We reported a similar weakness during our audit for fiscal year 2000-01. Please refer to reference number **2001-13-1** for additional information.

<sup>3</sup> We reviewed the status of this issue during our audit of fiscal year 2000-01 and found that the Employment Development Department had not yet fully developed documentation for all allocation codes. Therefore, we reported a similar weakness for these programs. Please refer to reference number **2001-2-1** for additional information.

<sup>4</sup> We reported a similar weakness in our audit of fiscal year 2000-01. Please refer to reference number **2001-9-5** for additional information.

<sup>5</sup> We reported a similar weakness in our audit of fiscal year 2000-01. Please refer to reference number **2001-12-4** for additional information.

<sup>6</sup> We reported a similar weakness in our audit of fiscal year 2000-01. Please refer to reference number **2001-12-5** for additional information.

<sup>7</sup> We reported a similar weakness in our audit of fiscal year 2000-01. Please refer to reference number **2001-13-3** for additional information.

<sup>8</sup> We reviewed the status of this issue during our audit of fiscal year 2000-01 and found that Education continued to use Migrant Education funds without always determining whether costs are reasonable as required by OMB Circular A-87. Therefore, we reported a similar weakness for this program. Please refer to reference number **2001-2-3** for additional information.

<sup>9</sup> We reported a similar weakness during our audit of fiscal year 2000-01. Please refer to reference number **2001-2-3** for additional information.

<sup>10</sup> We reviewed the status of this issue during our audit of fiscal year 2000-01 and found that the Chancellor's Office had not yet fully implemented adequate procedures to ensure that subrecipients minimize the time elapsing between their receipt and use of federal program funds. Therefore, we reported a similar weakness for this program. Please refer to **2001-3-8** for additional information.

<sup>11</sup> We reviewed the status of this issue during our audit of fiscal year 2000-01 and found that Alcohol and Drug Programs did not ensure that subrecipients minimized the time elapsing between their receipt and use of federal program funds. Therefore, we reported a similar weakness for this program. Please refer to reference number **2001-3-7** for additional information.

<sup>12</sup> We reported a similar weakness during our audit of fiscal year 2000-01. Please refer to reference number **2001-3-3** for additional information.

<sup>13</sup> We reported a similar weakness during our audit of fiscal year 2000-01. Please refer to reference number **2001-5-2** for additional information.

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<sup>14</sup> We reviewed the status of this issue during our audit of fiscal year 2000-01 and found that Alcohol and Drug Programs did not always ensure that charges to federal awards are within each award's period of availability. Therefore, we reported a similar weakness for fiscal year 2000-01. Please refer to reference number **2001-8-2** for additional information.

<sup>15</sup> We reported a similar weakness during our audit of fiscal year 2000-01. Please refer to **2001-14-3** for additional information.

<sup>16</sup> Our testing for fiscal year 2000-01 revealed a similar weakness; namely, the department did not obtain sufficient information from subrecipients related to the earmarking requirements. Please refer to reference number **2001-7-1** for additional information.

<sup>17</sup> Although Health Services modified its standard contract for fiscal year 2001-02 to include the suspension and debarment certification, it has not implemented procedures to obtain these certifications from its subrecipients for fiscal year 2000-01. Therefore, we reported a similar weakness in our audit of fiscal year 2000-01. Please refer to reference number **2001-9-2** for additional information.

<sup>18</sup> Although the Health Services added new footnotes to its annual report explaining that some of the amounts are based on estimates, it continues to not disclose that other amounts are based on estimates. Therefore, we reported a similar weakness in our audit of fiscal year 2000-01. Please refer to reference number **2001-12-1** for additional information.

<sup>19</sup> Health Services has completed only part of its effort to re-enroll the 140,000 providers of Medicaid services. Therefore, we reported a similar weakness for this program. Please refer to reference number **2001-14-4** for additional information.

*Agency's response provided as text only:*

Department of Finance  
Office of the Director  
State Capitol, Room 1145  
Sacramento, CA 95814-4998

March 12, 2002

Ms. Elaine M. Howle  
State Auditor  
555 Capitol Mall, Suite 300  
Sacramento, CA 95814

Dear Ms. Howle:

**State of California: Internal Control and State and Federal Compliance Audit Report  
For the Year Ended June 30, 2001**

Thank you for the opportunity to respond to the internal control and state and federal compliance audit report. This report was the result of your examination of the State's general purpose financial statements for the fiscal year ended June 30, 2001, and will be part of the Single Audit Report covering this period. We accept the reported findings and recommendations. Although our internal controls and administration of federal awards can always be improved, the conclusion that none of the findings were material weaknesses is evidence of the State's effective fiscal oversight.

California provides its citizens with numerous state and federal programs and activities and is much more complex and vast than most economic entities in the world. Such complexity, along with ever-present budget constraints, challenges us to meet the requirements of those programs and activities efficiently and effectively. Moreover, such operations must exist within a system of internal and administrative control that safeguards assets and resources and produces reliable financial information. Attaining these objectives and overseeing the financial and business practices of the State continues to be an important part of the Department of Finance's leadership.

In meeting our responsibility for financial leadership and oversight, the Department of Finance conducts internal control reviews of State departments and also reviews areas of potential weakness in the State's fiscal systems. In addition, we provide oversight of departmental internal audit units by issuing audit guidelines and conducting quality assurance reviews. Further, we have an ongoing process of issuing Audit Memos to departments that establish statewide policy and provide technical advice on various audit related issues. We will soon issue an Audit Memo concerning the results of the fiscal year 2000-01 Single Audit.

Ms. Elaine Howle  
March 12, 2002  
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The head of each State department is responsible for establishing and maintaining a system of internal accounting and administrative control within their department. This responsibility includes documenting the system, communicating system requirements to employees, and assuring that the system is functioning as prescribed and is modified for changing conditions.

Moreover, all levels of State management must be involved in assessing and strengthening their system of internal accounting and administrative controls to minimize fraud, errors, abuse, and waste of government funds.

Individual departments have separately responded to the report's findings and recommendations. Accordingly, their viewpoints and corrective action plans are included in the report. We will monitor the findings and reported corrective actions to identify potential changes in statewide fiscal procedures.

The Department of Finance will continue to provide leadership to ensure the proper financial operations and business practices of the State, and to ensure that internal controls exist for the safeguarding and effective use of assets and resources.

If you have any questions concerning this letter, please contact Samuel E. Hull, Chief, Office of State Audits and Evaluations, at (916) 322-2985.

Sincerely,

*(Signed by B. Timothy Gage)*

B. TIMOTHY GAGE  
Director

cc: Members of the Legislature  
Office of the Lieutenant Governor  
Milton Marks Commission on California State  
Government Organization and Economy  
Department of Finance  
Attorney General  
State Controller  
State Treasurer  
Legislative Analyst  
Senate Office of Research  
California Research Bureau  
Capitol Press