
Federal Findings and Questioned Costs

2018-002 **The Department of Social and Health Services improperly charged \$454,838 to the SNAP Cluster.**

Federal Awarding Agency: U.S. Department of Agriculture
Pass-Through Entity: None
CFDA Number and Title: 10.551 Supplemental Nutrition Assistance Program (SNAP)
10.561 State Administrative Matching Grants for SNAP
Federal Award Number: 7WA430WA5, 7WA430WA4, 7WA400WA4, 7WA4004WA
Applicable Compliance Component: Period of Performance
Known Questioned Cost Amount: \$454,838

Background

The Department of Social and Health Services (Department) administers the Supplemental Nutrition Assistance Program (SNAP) Cluster. The Department is responsible for ensuring grant money is used for costs that are allowable and related to each grant's purpose. Each federal grant specifies a performance period during which program costs may be obligated or liquidated. These periods typically align with the federal fiscal year of October 1 through September 30. Payments for costs charged before a grant's beginning date are not allowed without the grantor's prior approval.

The Department spent about \$1.4 billion in federal grant funds during fiscal year 2018.

The Department uses a financial system that is heavily automated and assigns expenditures to a specific grant year. In the prior four audits, we found that the Department improperly charged multiple federal grants before their beginning dates. These were reported as finding numbers 2017-002, 2016-002, 2015-003 and 2014-022.

During fiscal years 2017 and 2018, the Department implemented a new manual process to identify and move unallowable charges to the proper grant.

Description of Condition

The Department had adequate internal controls to ensure it materially complied with period of performance requirements. However, we found \$35,842 in expenditures were charged to the SNAP Cluster for activities that occurred before the grant was open. Additionally, we found \$418,996 that was obligated to the grant after the period of performance ended.

The Department did not have prior authorization from the grantor to charge these grants.

Cause of Condition

Management did not provide proper oversight to ensure all improper charges were identified and reversed by staff.

Effect of Condition and Questioned Costs

We are questioning improperly charged expenditures made to the SNAP Cluster as follows:

- \$35,842 made before the start of the performance period
- \$418,996 obligated to a grant after the period of performance ended

We question costs when we find an agency has not complied with grant regulations or when it does not have adequate documentation to support its expenditures.

Recommendations

We recommend the Department:

- Only charge expenditures to federal grants if they are obligated during the period of performance
- Consult with the grantor to discuss whether the questioned costs identified in the audit should be repaid

Department's Response

The Department concurs with this finding.

The Department immediately corrected the questioned costs by moving the improperly charged expenditures to the proper grant year via the journal voucher process.

In response to DSHS 2016-002 finding, the Department implemented a mandatory process for Economic Services Administration staff to include the Month of Service (MOS) on the Agency and Financial Reporting System (AFRS) transactions. The Department utilizes the MOS to perform a monthly review of AFRS transactions to identify unallowable charges and move them via the journal voucher process to the proper grant year. At the time of this audit, the Department did not have a process in place to ensure staff were following procedures to prevent Period of Performance issues.

In addition, the Department did not have tools in place to hold staff accountable.

The Department will update processes and procedures for management oversight to prevent future expenditures from being improperly charged to the wrong grant year. Management will:

- *Assign backup coverage during staff absences*

- *Review, on a monthly basis, the monthly monitoring accounting report and take action where appropriate*
- *Hold staff accountable through use of a monthly task list*
- *Meet with the Accounting and Internal Control Administrator monthly to brief her on period of performance status and oversight*

If the grantor contacts the Department regarding questioned costs that should be repaid, the Department will confirm these costs with the Department of Health & Human Services and will take appropriate action.

Auditor's Concluding Remarks

We thank the Department for its cooperation and assistance throughout the audit. We will review the status of the Department's corrective action during our next audit.

Applicable Laws and Regulations

Title 2 U.S. Code of Federal Regulations Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance) establishes the following applicable requirements:

Section 200.53 Improper Payments states:

- Improper payment* means any payment that should not have been made or that was made in an incorrect amount (including overpayments and underpayments) under statutory, contractual, administrative, or other legally applicable requirements; and
- Improper payment* includes any payment to an ineligible party, any payment for an ineligible good or service, any duplicate payment, any payment for a good or service not received (except for such payments where authorized by law), any payment that does not account for credit for applicable discounts, and any payment where insufficient or lack of documentation prevents a reviewer from discerning whether a payment was proper.

Section 200.403 Factors affecting Allowability of costs.

Except where otherwise authorized by statute, costs must meet the following general criteria in order to be allowable under Federal awards.

- Be necessary and reasonable for the performance of the Federal award and be allocable thereto under these principles.
- Conform to any limitations or exclusions set forth in these principles or in the Federal award as to types or amount of cost items.
- Be consistent with policies and procedures that apply uniformly to both federally-financed and other activities of the non-Federal entity.
- Be accorded consistent treatment. A cost may not be assigned to a Federal award as a direct cost if any other cost incurred for the same purpose in like circumstances has been allocated to the Federal award as an indirect cost.

- (e) Be determined in accordance with generally accepted accounting principles (GAAP), except, for state and local governments and Indian tribes only, as otherwise provided for in this part.
- (f) Not be included as a cost or used to meet cost sharing or matching requirements of any other federally-financed program in either the current or a prior period. See also §200.306 Cost sharing or matching paragraph (b).
- (g) Be adequately documented. See also §§200.300 Statutory and national policy requirements through 200.309 Period of performance of this part.

Section 200.410 Collection of unallowable costs.

Payments made for costs determined to be unallowable by either the Federal awarding agency, cognizant agency for indirect costs, or pass-through entity, either as direct or indirect costs, must be refunded (including interest) to the Federal Government in accordance with instructions from the Federal agency that determined the costs are unallowable unless Federal statute or regulation directs otherwise. See also Subpart D—Post Federal Award Requirements of this part, §§200.300 Statutory and national policy requirements through 200.309 Period of performance.

Section 200.516 Audit findings, states in part:

- (a) *Audit findings reported.* The auditor must report the following as audit findings in a schedule of findings and questioned costs:
 - (3) Known questioned costs that are greater than \$25,000 for a type of compliance requirement for a major program. Known questioned costs are those specifically identified by the auditor. In evaluating the effect of questioned costs on the opinion on compliance, the auditor considers the best estimate of total costs questioned (likely questioned costs), not just the questioned costs specifically identified (known questioned costs). The auditor must also report known questioned costs when likely questioned costs are greater than \$25,000 for a type of compliance requirement for a major program. In reporting questioned costs, the auditor must include information to provide proper perspective for judging the prevalence and consequences of the questioned costs.

Section 200.309 Period of performance, states:

A non-Federal entity may charge to the Federal award only allowable costs incurred during the period of performance and any costs incurred before the Federal awarding agency or pass-through entity made the Federal award that were authorized by the Federal awarding agency or pass-through entity.

Title 2 U.S. Code of Federal Regulations Part 200, Appendix XI Compliance Supplement, states in part:

H. Period of Performance

Compliance Requirements

A non-Federal entity may charge to the Federal award only allowable costs incurred during the period of performance and any costs incurred before the Federal awarding agency or pass-through entity made the Federal award that were authorized by the Federal awarding agency or pass-through entity (2 CFR section 200.309).

Unless the Federal awarding agency or pass-through entity authorizes an extension, a non-Federal entity must liquidate all obligations incurred under the Federal award not later than 90 calendar days after the end date of the period of performance as specified in the terms and conditions of the Federal award (2 CFR section 200.343(b)). When used in connection with a non-Federal entity's utilization of funds under a Federal award, "obligations" means orders placed for property and services, contracts and subawards made, and similar transactions during a given period that require payment by the non-Federal entity during the same or a future period (2 CFR section 200.71).

The Department spent about \$117 million in federal grant funds during fiscal year 2018, including about \$66 million paid in food benefits to WIC clients.

Description of Condition

We found the Department had adequate internal controls to ensure it materially complied with eligibility requirements.

We used a statistical sampling method to randomly select and examine 59 clients of a total population of 220,264. We reviewed each client's records and determined that 58 of the 59 clients were eligible to receive benefits. In one instance, a client was issued checks for the month following the end of their grace period without providing proof of identification/residency and income. Proof of identification/residency and income was later provided, however it was after a second set of checks was issued and after the one month grace period. This resulted in known questioned costs of \$151.

Federal regulations require the auditor to issue a finding when the known or estimated questioned costs identified in a single audit exceed \$25,000. We are issuing this finding because, as stated in the Effect of Condition and Questioned Cost section of this finding, the estimated questioned costs exceed that threshold.

This condition was not reported in the prior audit.

Cause of Condition

Staff at the WIC clinic did not require the client to provide proof of identification/residency and income before issuing a second set of checks. The case management system does not automatically discontinue the client's eligibility determination after the grace period expires.

Effect of Condition and Questioned Costs

A statistical sampling method was used to randomly select the payments in the audit. We estimate the amount of likely improper federal payments to be \$565,257.

Our sampling methodology meets statistical sampling criteria under generally accepted auditing standards in AU-C 530.05. It is important to note that the sampling technique we used is intended to support our audit conclusions by determining if expenditures complied with program requirements in all material respects. Accordingly, we used an acceptance sampling formula designed to provide a high level of assurance, with a 95 percent confidence of whether exceptions exceeded our materiality threshold. Our audit report and finding reflects this conclusion. However, the likely improper payment projections are a point estimate and only represent our "best estimate of total questioned costs" as required by 2 CFR 200.516(3).

We question costs when we find an agency has not complied with grant regulations or when it does not have adequate documentation to support its expenditures.

Recommendations

We recommend the Department:

- Ensure WIC clinic staff understand and follow all the requirements and procedures for verifying proof of eligibility before issuing checks to clients
- Consult with the grantor to discuss whether the known questioned costs identified in the audit should be repaid

Department's Response

Thank you for making us aware of this issue. We will remind our local agencies and provide training and technical assistance where needed about policies related to this issue.

The WIC program has been working on a new electronic system, Cascades MIS, which will address this issue. The system will be on boarded on March 4, 2019 and rolled out fully by October 31, 2019. The system moves away from manual check printing and instead utilizes an EBT card. The new system has safeguards built into it that prevent funds from being issued to clients if proof of identity/residence and verification of income is not entered into the system.

Auditor's Concluding Remarks

We thank the Department for its cooperation and assistance throughout the audit. We will review the status of the Department's corrective action during our next audit.

Applicable Laws and Regulations

Title 2 U.S. Code of Federal Regulations Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance) establishes the following applicable requirements:

Section 200.53 Improper Payments states:

- (a) *Improper payment* means any payment that should not have been made or that was made in an incorrect amount (including overpayments and underpayments) under statutory, contractual, administrative, or other legally applicable requirements; and
- (b) *Improper payment* includes any payment to an ineligible party, any payment for an ineligible good or service, any duplicate payment, any payment for a good or service not received (except for such payments where authorized by law), any payment that does not account for credit for applicable discounts, and any payment where insufficient or lack of documentation prevents a reviewer from discerning whether a payment was proper.

Section 200.403 Factors affecting Allowability of costs.

Except where otherwise authorized by statute, costs must meet the following general criteria in order to be allowable under Federal awards.

- (a) Be necessary and reasonable for the performance of the Federal award and be allocable thereto under these principles.
- (b) Conform to any limitations or exclusions set forth in these principles or in the Federal award as to types or amount of cost items.
- (c) Be consistent with policies and procedures that apply uniformly to both federally-financed and other activities of the non-Federal entity.
- (d) Be accorded consistent treatment. A cost may not be assigned to a Federal award as a direct cost if any other cost incurred for the same purpose in like circumstances has been allocated to the Federal award as an indirect cost.
- (e) Be determined in accordance with generally accepted accounting principles (GAAP), except, for state and local governments and Indian tribes only, as otherwise provided for in this part.
- (f) Not be included as a cost or used to meet cost sharing or matching requirements of any other federally-financed program in either the current or a prior period. See also §200.306 Cost sharing or matching paragraph (b).
- (g) Be adequately documented. See also §§200.300 Statutory and national policy requirements through 200.309 Period of performance of this part.

Section 200.410 Collection of unallowable costs.

Payments made for costs determined to be unallowable by either the Federal awarding agency, cognizant agency for indirect costs, or pass-through entity, either as direct or indirect costs, must be refunded (including interest) to the Federal Government in accordance with instructions from the Federal agency that determined the costs are unallowable unless Federal statute or regulation directs otherwise. See also Subpart D—Post Federal Award Requirements of this part, §§200.300 Statutory and national policy requirements through 200.309 Period of performance.

Section 200.516 Audit findings, states in part:

- (a) *Audit findings reported.* The auditor must report the following as audit findings in a schedule of findings and questioned costs:
 - (3) Known questioned costs that are greater than \$25,000 for a type of compliance requirement for a major program. Known questioned costs are those specifically identified by the auditor. In evaluating the effect of questioned costs on the opinion on compliance, the auditor considers the best estimate of total costs questioned (likely questioned costs), not just the questioned costs specifically identified (known questioned costs). The auditor must also report known questioned costs when likely questioned costs are greater than \$25,000 for a type of compliance requirement for a major program. In reporting questioned costs, the auditor must include information to provide proper perspective for judging the prevalence and consequences of the questioned costs.

Title 7 U.S. Code of Federal Regulations Section 246.7 Certification of participants, states in part:

(c) *Eligibility criteria and basic certification procedures.*

(1) To qualify for the Program, infants, children, and pregnant, postpartum, and breastfeeding women must:

(i) Reside within the jurisdiction of the State (except for Indian State agencies). Indian State agencies may establish a similar requirement. All State agencies may determine a service area for any local agency, and may require that an applicant reside within the service area. However, the State agency may not use length of residency as an eligibility requirement.

(ii) Meet the income criteria specified in paragraph (d) of this section.

(iii) Meet the nutritional risk criteria specified in paragraph (e) of this section.

(2)(i) At certification, the State or local agency must require each applicant to present proof of residency (i.e., location or address where the applicant routinely lives or spends the night) and proof of identity. The State or local agency must also check the identity of participants, or in the case of infants or children, the identity of the parent or guardian, or proxies when issuing food, cash-value vouchers or food instruments. The State agency may authorize the certification of applicants when no proof of residency or identity exists (such as when an applicant or an applicant's parent is a victim of theft, loss, or disaster; a homeless individual; or a migrant farmworker). In these cases, the State or local agency must require the applicant to confirm in writing his/her residency or identity. Further, an individual residing in a remote Indian or Native village or an individual served by an Indian tribal organization and residing on a reservation or pueblo may establish proof of residency by providing the State agency their mailing address and the name of the remote Indian or Native village.

(d) *Income criteria and income eligibility determinations.* The State agency shall establish, and provide local agencies with, income guidelines, definitions, and procedures to be used in determining an applicant's income eligibility for the Program.

(2) *Income eligibility determinations.* The State agency shall ensure that local agencies determine income through the use of a clear and simple application form provided or approved by the State agency.

(v) *Are applicants required to document income eligibility?*

(A) *Adjunctively/automatically income eligible applicants.* The State or local agency must require applicants determined to be adjunctively or automatically income eligible to document their eligibility for the program that makes them income eligible as set forth in paragraph (d)(2)(vi) of this section.

(B) *Other applicants.* The State or local agency must require all other applicants to provide documentation of family income at certification.

Washington State WIC Manual, states in part:

Chapter 3, Section 3, One Month Grace Period for Proof of Identification or Residency.

Staff must allow a one month grace period for proof of identification or residency.

Staff must document on the Income Documentation tab when the client doesn't provide client identification or proof of residency at the certification or transfer in appointment.

Staff must see and document the missing proof before giving additional WIC checks past the one month grace period.

Chapter 6, Section 5 Documenting Income Information, states in part:

Staff must screen for income eligibility based on the self-reported amount when the applicant, client or caregiver doesn't bring proof of income or proof of participation for an income-qualifying program to the certification appointment.

If the self-reported amount meets WIC income guidelines, staff:

1. Document the self-reported amount on the Grace Period for Proof of Income form and have the person sign.
2. Provide a one month grace period for the proof.
3. Issue one set of checks.

Staff can use one Grace Period for Proof of Income form for household members who are certified and given a grace period for proof of income on the same day.

Staff must document the proof as "Not Provided" in the applicant's or client's file. This automatically documents the one month grace period.

The person must bring in the missing proof showing WIC income eligibility before staff provide a second set of WIC checks.

2018-004 The Department of Health improperly charged \$31,051 to the Special Supplemental Nutrition Program for Women, Infants and Children grant.

Federal Awarding Agency: Department of Agriculture, Food and Nutrition Service
Pass-Through Entity: None
CFDA Number and Title: 10.557 Special Supplemental Nutrition Program for Women, Infants and Children (WIC)
Federal Award Number: 177WAWA7W1003;177WAWA7W1006; 187WAWA7W1003; 187WAWA7W1006;
Applicable Compliance Component: Activities Allowed/Unallowed Allowable Costs/Cost Principles
Known Questioned Cost Amount: \$ 31,051

Background

The Department of Health (Department) operates the Special Supplemental Nutrition Program for Women, Infants and Children (WIC). WIC reaches more than 274,000 women and children in over 200 clinics throughout the state and is funded exclusively with federal grants from the U.S. Department of Agriculture.

WIC serves pregnant, postpartum and breastfeeding women, and children up to 5 years old, who are at or below 185 percent of the federal poverty level. WIC provides:

- Nutrition ideas and tips on how to eat well and be more active
- Breastfeeding support, such as access to a peer counselor (varies by agency)
- Health reviews and referrals
- Monthly checks for healthy food, such as fruit, vegetables and milk, and fortified formula

Department employees who work 100 percent of their time on a single grant for a period of three months during the year are not required to submit timesheets. Instead, their supervisor submits a quarterly time certification form that shows the grant to which the employee’s salary is charged. A fiscal employee prepares the certification forms and sends them to WIC program staff to be completed by the supervisor. According to Department policy, quarterly time certifications must be submitted by the 30th day of the month following the end of the applicable quarter. Employees who work on additional activities other than the grant program must complete a timesheet twice a month.

The Department spent about \$117 million in federal grant funds during fiscal year 2018, with about \$7 million paid in salaries and benefits to Department employees.

Description of Condition

The Department improperly charged \$31,051 in salaries and benefits to the WIC grant.

The Department had adequate internal controls to ensure it materially complied with the activities allowed compliance requirement.

We found one instance when an employee did not submit a certification timely. The employee's, certification for the January – March 2018 quarter was due by April 30, 2018, but was not submitted until July 2018.

This condition was not reported in the prior audit.

Cause of Condition

The quarterly certification was not completed in a timely manner due to an oversight by Department staff.

Effect of Condition and Questioned Costs

Because the employee's time certification was not completed in a timely manner, we determined the Department improperly charged \$31,051 in salaries and benefits to the WIC grant.

We question costs when we find an agency has not complied with grant regulations or when it does not have adequate documentation to support its expenditures.

Recommendations

We recommend the Department:

- Ensure quarterly time certifications are submitted in a timely manner
- Consult with the grantor to discuss whether the questioned costs identified in the audit should be repaid

Department's Response

Thank you for making us aware of this issue.

We understand that this finding was the result of one quarterly time certification that was submitted after the 30th day following the end of the quarter, as required by Department policy.

With the awareness of this issue, we will review our policies, as well as our procedures and processes, to determine if updates are necessary in an effort to ensure we meet the needs of the Department and Federal requirements.

The Department will also provide training to staff, to include any changes that are made to policies, procedures and/or processes.

Auditor's Concluding Remarks

We thank the Department for its cooperation and assistance throughout the audit. We will review the status of the Department's corrective action during our next audit.

Applicable Laws and Regulations

Title 2 U.S. Code of Federal Regulations Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance) establishes the following applicable requirements:

Section 200.53 Improper Payments states:

- (a) *Improper payment* means any payment that should not have been made or that was made in an incorrect amount (including overpayments and underpayments) under statutory, contractual, administrative, or other legally applicable requirements; and
- (b) *Improper payment* includes any payment to an ineligible party, any payment for an ineligible good or service, any duplicate payment, any payment for a good or service not received (except for such payments where authorized by law), any payment that does not account for credit for applicable discounts, and any payment where insufficient or lack of documentation prevents a reviewer from discerning whether a payment was proper.

Section 200.403 Factors affecting Allowability of costs.

Except where otherwise authorized by statute, costs must meet the following general criteria in order to be allowable under Federal awards.

- (a) Be necessary and reasonable for the performance of the Federal award and be allocable thereto under these principles.
- (b) Conform to any limitations or exclusions set forth in these principles or in the Federal award as to types or amount of cost items.
- (c) Be consistent with policies and procedures that apply uniformly to both federally-financed and other activities of the non-Federal entity.
- (d) Be accorded consistent treatment. A cost may not be assigned to a Federal award as a direct cost if any other cost incurred for the same purpose in like circumstances has been allocated to the Federal award as an indirect cost.
- (e) Be determined in accordance with generally accepted accounting principles (GAAP), except, for state and local governments and Indian tribes only, as otherwise provided for in this part.
- (f) Not be included as a cost or used to meet cost sharing or matching requirements of any other federally-financed program in either the current or a prior period. See also §200.306 Cost sharing or matching paragraph (b).
- (g) Be adequately documented. See also §§200.300 Statutory and national policy requirements through 200.309 Period of performance of this part.

Section 200.410 Collection of unallowable costs.

Payments made for costs determined to be unallowable by either the Federal awarding agency, cognizant agency for indirect costs, or pass-through entity, either as direct or indirect costs, must be refunded (including interest) to the Federal Government in accordance with instructions from the Federal agency that determined the costs are unallowable unless Federal statute or regulation directs otherwise. See also Subpart D—Post Federal Award Requirements of this part, §§200.300 Statutory and national policy requirements through 200.309 Period of performance.

Section 200.516 Audit findings, states in part:

- (a) *Audit findings reported.* The auditor must report the following as audit findings in a schedule of findings and questioned costs:
 - (3) Known questioned costs that are greater than \$25,000 for a type of compliance requirement for a major program. Known questioned costs are those specifically identified by the auditor. In evaluating the effect of questioned costs on the opinion on compliance, the auditor considers the best estimate of total costs questioned (likely questioned costs), not just the questioned costs specifically identified (known questioned costs). The auditor must also report known questioned costs when likely questioned costs are greater than \$25,000 for a type of compliance requirement for a major program. In reporting questioned costs, the auditor must include information to provide proper perspective for judging the prevalence and consequences of the questioned costs.

Section 200.430 Compensation—personal services, states in part:

- (a) *General.* Compensation for personal services includes all remuneration, paid currently or accrued, for services of employees rendered during the period of performance under the Federal award, including but not necessarily limited to wages and salaries. Compensation for personal services may also include fringe benefits which are addressed in § 200.431 Compensation—fringe benefits. Costs of compensation are allowable to the extent that they satisfy the specific requirements of this part, and that the total compensation for individual employees:
 - (1) Is reasonable for the services rendered and conforms to the established written policy of the non-Federal entity consistently applied to both Federal and non-Federal activities;
 - (3) Is determined and supported as provided in paragraph (i) of this section, Standards for Documentation of Personnel Expenses, when applicable.
- (i) Allowable activities. Charges to Federal awards may include reasonable amounts for activities contributing and directly related to work under an agreement, such as delivering special lectures about specific aspects of the ongoing activity, writing reports and articles, developing and maintaining protocols (human, animals, etc.), managing substances/chemicals, managing and securing project-specific data, coordinating research subjects, participating in appropriate seminars, consulting with colleagues and graduate students, and attending meetings and conferences.

Department of Health, Procedure(s) 11.014 Time and Effort Requirements for Federal Grant Funding, states in part:

Timekeeping for Federal Requirements:

To satisfy the federal requirements in 2 CFR Part 200, all employees who are in one or more of the categories listed below must complete a semi-monthly Timekeeping (TK) time sheet. For employees funded from a single federal award or cost objective, a Quarterly Timekeeping Certification can be used in lieu of the semi-monthly PTA form.

Definitions:

Federal award includes federal financial assistance when the Department of Health is the prime recipient or sub recipient.

Cost objective means a program, function, activity, award, organizational subdivision, contract, or work unit for which cost data are desired and for which provision is made to accumulate and measure the costs of processes, product jobs, capital projects, etc. A cost objective may be a major function of the non-federal entity, a particular service or project, a federal award, or an indirect cost activity, as described in subpart E-Costs Principles of this part. (2 CFR Part 200.28)

Process: Federal Timekeeping Using Quarterly Time Certifications

Employees who are funded by a single federal grant or cost objective may complete a quarterly time certification of time spent in the activity to which they are charged in lieu of a semi-monthly timekeeping sheet. For quarterly time certification, a single federal grant or cost objective may include state or local match or cost share for the federal grant or cost objective.

1. Supervisor will inform employee of the method of time keeping reporting to use for federal timekeeping and provide a copy of procedure 11.014. (Supervisor, Employee)
2. Payroll and Related reports for each pay period within the quarter will be reviewed. A consolidated list of employees who need to submit a quarterly timekeeping certification will be identified. (Grants)
3. An email notification will be sent to the Attendance Keepers and cc'd to the Finance Operations Group. The email will include a copy of the quarterly certification form. (Grants)
4. Complete the quarterly timekeeping certification and submit to supervisor for approval. (Attendance Keeper)
5. Review, verify accuracy, resolve questions, then sign the quarterly time certification form and submit to program Attendance Keeper. (Supervisor)
6. Email the completed quarterly time certification form to (centralized email address). The completed form is due by the 30th of the following month after the calendar quarter ends. (Attendance Keeper)
7. The receipt of completed quarterly certification forms will be tracked by Financial Services. Supervisors and Attendance Keepers that have not submitted the certifications by the due date will be notified. (Grants)

2018-005 **The Department of Health did not have adequate internal controls over and did not comply with federal requirements to ensure subrecipients of the Special Supplemental Nutrition Program for Women, Infants, and Children program received required audits.**

Federal Awarding Agency: Department of Agriculture, Food and Nutrition Service
Pass-Through Entity: None
CFDA Number and Title: 10.557 Special Supplemental Nutrition Program for Women, Infants, and Children (WIC)
Federal Award Number: 177WAWA7W1003;177WAWA7W1006;
187WAWA7W1003; 187WAWA7W1006;
Applicable Compliance Component: Subrecipient Monitoring
Known Questioned Cost Amount: \$0

Background

The Department of Health (Department) operates the Special Supplemental Nutrition Program for Women, Infants and Children (WIC). WIC reaches more than 274,000 women and children in over 200 clinics throughout the state and is funded exclusively with federal grants from the U.S. Department of Agriculture.

WIC serves pregnant, postpartum and breastfeeding women, and children up to 5 years old, who are at or below 185 percent of the federal poverty level. WIC provides:

- Nutrition ideas and tips on how to eat well and be more active
- Breastfeeding support, such as access to a peer counselor (varies by agency)
- Health reviews and referrals
- Monthly checks for healthy food, such as fruit, vegetables and milk, and fortified formula

Federal regulations require the Department to monitor the activities of award subrecipients. This includes ensuring its subrecipients that spend \$750,000 or more in federal grant money during a fiscal year obtain a single audit. The audit must be completed and submitted to the Federal Audit Clearinghouse no later than nine months after the end of the subrecipient’s fiscal year. The Department also must follow up on any audit findings a subrecipient receives that might affect the federal program, and must issue a management decision within six months of the audit report’s acceptance by the Federal Audit Clearinghouse. These requirements help ensure grant money is used for authorized purposes and within the provisions of contracts or grant agreements.

The Department spent about \$117 million in federal grant funds during fiscal year 2018, and it passed through about \$33 million to local WIC agencies as subrecipients of grant funds.

Description of Condition

The Department of Health did not have adequate internal controls in place to verify:

- Subrecipients received required audits
- Findings for the WIC program were followed up on and management decisions were issued promptly

The Department uses a spreadsheet to track subrecipient audit activity, including whether or not the subrecipient required an audit and if review of an audit was performed by Department staff. However, the spreadsheet did not include any information on the subrecipients' fiscal year end, when the audit would be due by, the Federal Audit Clearinghouse acceptance date or when the Department would need to perform and complete its review and issue a management decision. We determined the tracking spreadsheet was not an effective internal control to monitor whether subrecipients received federal audits as required.

We reviewed 17 out of 58 subrecipients required to have a single audit during our scope and determined all 17 received an audit. However, we found nine of 17 audits were not reviewed by the Department within six months of issuance to determine if there were any findings and to issue a management decision if required. We verified that one of the audits had a finding related to client eligibility that required the Department to issue a management decision.

We consider these internal control deficiencies to be a material weakness.

This condition was not reported in the prior audit.

Cause of Condition

Although the Department had a written process to monitor and verify if subrecipients received audits, it did not provide adequate instruction to staff who were assigned this responsibility.

The employee who began the monitoring process during the audit period retired in July 2017. Another employee in the grants management unit was assigned to take over this responsibility, but was not properly trained to ensure they understood how to monitor the subrecipients.

Due to turnover and shortage of staff in the grants management unit from July 2017 through March 2018, the workload increased for all remaining employees, so the monitoring of subrecipient audit activity was not performed consistently or in a timely manner.

Effect of Condition

Without establishing adequate internal controls, the Department cannot ensure all subrecipients that met the threshold for an audit complied with federal grant requirements. In addition, one subrecipient received an audit finding that the Department did not issue a management decision on, as required.

Recommendations

We recommend the Department:

- Ensure staff are properly trained and understand how to monitor and verify whether subrecipients received the required audits
- Receive and review all required audits within the required timeframes
- Follow up on all subrecipient audit findings related to the program and issue a management decision promptly

Department's Response

Thank you. We concur with the recommendations.

The department will review and update agency processes to ensure DOH receives and reviews required subrecipient audits and completes any follow up action within the required time frame. The department will provide clear guidance and additional training to staff to ensure a clear understanding of the process and related expectations.

In addition, the department will review and update the agency tracking spreadsheet that documents when and how each of the required actions are satisfied.

Auditor's Concluding Remarks

We thank the Department for its cooperation and assistance throughout the audit. We will review the status of the Department's corrective action during our next audit.

Applicable Laws and Regulations

Title 2 U.S. Code of Federal Regulations Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance) establishes the following applicable requirements:

Section 200.303 Internal controls, states in part:

The non-Federal entity must:

- (a) Establish and maintain effective internal control over the Federal award that provides reasonable assurance that the non-Federal entity is managing the Federal award in compliance with Federal statutes, regulations, and the terms and conditions of the Federal award. These internal controls should be in compliance with guidance in "Standards for Internal Control in the Federal Government" issued by the Comptroller General of the United States or the "Internal Control Integrated Framework", issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).
- (b) Comply with Federal statutes, regulations, and the terms and conditions of the Federal awards.

- (d) Take prompt action when instances of noncompliance are identified including noncompliance identified in audit findings.

Section 200.516 Audit findings, states in part:

- (a) *Audit findings reported.* The auditor must report the following as audit findings in a schedule of findings and questioned costs:
 - (1) Significant deficiencies and material weaknesses in internal control over major programs and significant instances of abuse relating to major programs. The auditor's determination of whether a deficiency in internal control is a significant deficiency or material weakness for the purpose of reporting an audit finding is in relation to a type of compliance requirement for a major program identified in the Compliance Supplement.
 - (2) Material noncompliance with the provisions of Federal statutes, regulations, or the terms and conditions of Federal awards related to a major program. The auditor's determination of whether a noncompliance with the provisions of Federal statutes, regulations, or the terms and conditions of Federal awards is material for the purpose of reporting an audit finding is in relation to a type of compliance requirement for a major program identified in the compliance supplement.

Section 200.331 Requirements for pass-through entities, states in part:

- (d) Monitor the activities of the subrecipient as necessary to ensure that the subaward is used for authorized purposes, in compliance with Federal statutes, regulations, and the terms and conditions of the subaward; and that subaward performance goals are achieved. Pass-through entity monitoring of the subrecipient must include:
 - (3) Issuing a management decision for audit findings pertaining to the Federal award provided to the subrecipient from the pass-through entity as required by §200.521 Management decision.
- (f) Verify that every subrecipient is audited as required by Subpart F—Audit Requirements of this part when it is expected that the subrecipient's Federal awards expended during the respective fiscal year equaled or exceeded the threshold set forth in §200.501 Audit requirements.

The American Institute of Certified Public Accountants defines significant deficiencies and material weaknesses in internal controls over compliance in its *Codification of Statements on Auditing Standards*, section 935, Compliance Audits, as follows:

- .11 For purposes of adapting GAAS to a compliance audit, the following terms have the meanings attributed as follows: ...

Deficiency in internal control over compliance. A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance on a timely basis. A deficiency in design exists when (a) a control necessary to meet the control objective is missing, or (b) an existing control is not properly designed so that, even if the control operates as designed, the control objective would not be met. A deficiency in operation exists when a properly designed

control does not operate as designed or the person performing the control does not possess the necessary authority or competence to perform the control effectively.

Material weakness in internal control over compliance. A deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a compliance requirement will not be prevented, or detected and corrected, on a timely basis. In this section, a reasonable possibility exists when the likelihood of an event occurring is either reasonably possible or probable as defined as follows:

Reasonably possible. The chance of the future event or events occurring is more than remote but less than likely.

Probable. The future event or events are likely to occur.

Significant deficiency in internal control over compliance. A deficiency, or a combination of deficiencies, in internal control over compliance that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

Material noncompliance. In the absence of a definition of material noncompliance in the governmental audit requirement, a failure to follow compliance requirements or a violation of prohibitions included in the applicable compliance requirements that results in noncompliance that is quantitatively or qualitatively material, either individually or when aggregated with other noncompliance, to the affected government program.

2018-006 **The Department of Health did not have adequate internal controls over and was not compliant with cash management requirements for the Special Supplemental Nutrition Program for Women, Infants and Children grant.**

Federal Awarding Agency: Department of Agriculture, Food and Nutrition Service
Pass-Through Entity: None
CFDA Number and Title: 10.557 Special Supplemental Nutrition Program for Women, Infants and Children (WIC)
Federal Award Number: 177WAWA7W1003;177WAWA7W1006;
187WAWA7W1003; 187WAWA7W1006;
Applicable Compliance Component: Cash Management
Known Questioned Cost Amount: \$0

Background

The Department of Health (Department) operates the Special Supplemental Nutrition Program for Women, Infants and Children (WIC). WIC reaches more than 274,000 women and children in over 200 clinics throughout the state and is funded exclusively with federal grants from the U.S. Department of Agriculture.

WIC serves pregnant, postpartum and breastfeeding women, and children up to 5 years old, who are at or below 185 percent of the federal poverty level. WIC provides:

- Nutrition ideas and tips on how to eat well and be more active
- Breastfeeding support, such as access to a peer counselor (varies by agency)
- Health reviews and referrals
- Monthly checks for healthy food, such as fruit, vegetables and milk, and fortified formula

The primary purpose of the Cash Management Improvement Act (CMIA) agreement is to ensure states request federal funds exactly when they are needed and that no interest is gained or lost by either the federal or state governments. The agreement specifies the funding technique the Department is to use when requesting federal funds. For the WIC program, the Department draws funds semi-monthly according to the state payroll schedule for program administrative costs and payments to providers, and daily for food benefit payments offset by manufacturer rebates. When the rebate balance is large enough to cover the balance for the food benefit payment, a draw is not necessary.

United Community Bank acts as the state’s fiscal agent and pays the food benefit expenditures. The Department executes a wire transfer every day for the preceding day’s food benefit using state dollars. The amount that is wired to the bank each day is the amount the Department should request to be reimbursed for in the daily draw.

The Department spent about \$117 million in federal grant funds during fiscal year 2018, with about \$66 million paid in food benefits to WIC clients, and \$51 million in administrative costs and payments to providers.

Description of Condition

The Department did not have adequate internal controls over and was not compliant with cash management requirements for the Special Supplemental Nutrition Program for Women, Infants and Children grant.

When the Department drew federal funds, it ensured the amounts drawn were correct based on actual payments. However, the Department did not monitor its federal drawdown frequency to ensure it complied with the CMIA. We determined 24 semi-monthly and 230 daily draws (depending on the available rebate balance) should have occurred during state fiscal year 2018. We randomly selected and examined 16 out of the 106 actual daily draws the Department performed during the year and all 14 semi-monthly draws that were done during the year. We found:

- Ten of the 16 daily draws were not drawn in a timely manner, including one draw that was 32 days late. Nine of the draws were a combination of two or more separate food benefit payments. The draw that was 32 days late should have been 18 separate daily draws, rather than one combined draw. The amounts that were drawn late ranged from \$241,298 to \$6,267,434.
- Eleven of the 14 semi-monthly draws we examined were not drawn on the state payroll schedule as required. We also determined that there were no semi-monthly draws made in July 2017, August 2017, February 2018 or April 2018.

In addition, the Department discovered it was overdrawn by \$121,359, but did not correct the error for two and a half months.

We consider these internal control deficiencies to be a material weakness.

This condition was not reported in the prior audit.

Cause of Condition

The Department experienced significant turnover during the audit period and believed it did not have the resources necessary to ensure draws were made in accordance with the CMIA.

Effect of Condition

Violations of the CMIA can result in the grantor denying the state payment or credit for the resulting federal interest liability or other sanctions. Delaying federal drawdown requests also results in state funds being advanced longer than necessary and lost interest revenue for the state.

Recommendations

We recommend the Department:

- Improve its internal controls to ensure cash draws are performed in accordance with the state’s CMIA agreement
- Train staff adequately to ensure federal draws are performed in a timely manner

Department’s Response

Thank you. We concur with the recommendations.

The Department will review and update the documented procedures and train staff to ensure compliance with Federal and CMIA requirements.

Auditor’s Concluding Remarks

We thank the Department for its cooperation and assistance throughout the audit. We will review the status of the Department’s corrective action during our next audit.

Applicable Laws and Regulations

Title 2 U.S. Code of Federal Regulations Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance) establishes the following applicable requirements:

Section 200.303 Internal controls, states in part:

The non-Federal entity must:

- (a) Establish and maintain effective internal control over the Federal award that provides reasonable assurance that the non-Federal entity is managing the Federal award in compliance with Federal statutes, regulations, and the terms and conditions of the Federal award. These internal controls should be in compliance with guidance in “Standards for Internal Control in the Federal Government” issued by the Comptroller General of the United States or the “Internal Control Integrated Framework”, issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).
- (b) Comply with Federal statutes, regulations, and the terms and conditions of the Federal awards.
- (d) Take prompt action when instances of noncompliance are identified including noncompliance identified in audit findings.

Section 200.516 Audit findings, states in part:

- (a) *Audit findings reported.* The auditor must report the following as audit findings in a schedule of findings and questioned costs:
 - (1) Significant deficiencies and material weaknesses in internal control over major programs and significant instances of abuse relating to major programs. The auditor’s determination of whether a deficiency in internal control is a significant deficiency or material weakness for the purpose of reporting an audit finding is in relation to a type of compliance requirement for a major program identified in the Compliance Supplement.

- (2) Material noncompliance with the provisions of Federal statutes, regulations, or the terms and conditions of Federal awards related to a major program. The auditor's determination of whether a noncompliance with the provisions of Federal statutes, regulations, or the terms and conditions of Federal awards is material for the purpose of reporting an audit finding is in relation to a type of compliance requirement for a major program identified in the compliance supplement.

Title 31 Code of Federal Regulations part 205.29 What are the State oversight and compliance responsibilities?, states in part:

- (d) If a State repeatedly or deliberately fails to request funds in accordance with the procedures established for its funding techniques, as set forth in § 205.11, § 205.12, or a Treasury-State agreement, we may deny the State payment or credit for the resulting Federal interest liability, notwithstanding any other provision of this part.
- (e) If a State materially fails to comply with this subpart A, we may, in addition to the action described in paragraph (d) of this section, take one or more of the following actions, as appropriate under the circumstances:
 - (1) Deny the reimbursement of all or a part of the State's interest calculation cost claim;
 - (2) Send notification of the non-compliance to the affected Federal Program Agency for appropriate action, including, where appropriate, a determination regarding the impact of non-compliance on program funding;
 - (3) Request a Federal Program Agency or the General Accounting Office to conduct an audit of the State to determine interest owed to the Federal government, and to implement procedures to recover such interest;
 - (4) Initiate a debt collection process to recover claims owed to the United States; or
 - (5) Take other remedies legally available.

The American Institute of Certified Public Accountants defines significant deficiencies and material weaknesses in internal controls over compliance in its *Codification of Statements on Auditing Standards*, section 935, Compliance Audits, as follows:

.11 For purposes of adapting GAAS to a compliance audit, the following terms have the meanings attributed as follows: ...

Deficiency in internal control over compliance. A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance on a timely basis. A deficiency in design exists when (a) a control necessary to meet the control objective is missing, or (b) an existing control is not properly designed so that, even if the control operates as designed, the control objective would not be met. A deficiency in operation exists when a properly designed control does not operate as designed or the person performing the control does not possess the necessary authority or competence to perform the control effectively.

Material weakness in internal control over compliance. A deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a compliance requirement will not be prevented, or detected and corrected, on a timely basis. In this section, a reasonable possibility exists when

the likelihood of an event occurring is either reasonably possible or probable as defined as follows:

Reasonably possible. The chance of the future event or events occurring is more than remote but less than likely.

Probable. The future event or events are likely to occur.

Significant deficiency in internal control over compliance. A deficiency, or a combination of deficiencies, in internal control over compliance that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

Material noncompliance. In the absence of a definition of material noncompliance in the governmental audit requirement, a failure to follow compliance requirements or a violation of prohibitions included in the applicable compliance requirements that results in noncompliance that is quantitatively or qualitatively material, either individually or when aggregated with other noncompliance, to the affected government program.

The Cash Management Improvement Act (CMIA) of 2018, states in part:

6.2 Description of Funding Techniques, 6.2.1: The following are terms under which standard funding techniques shall be implemented for all transfers of funds to which the funding technique is applied in section 6.3.2 of this Agreement.

Actual Clearance, ZBA - ACH

The State shall request funds such that they are deposited by ACH in a State account on the settlement date of payments issued by the State. The request shall be made in accordance with the appropriate Federal agency cut-off time specified in Exhibit I. The amount of the request shall be for the amount of funds that clear the State's account on the settlement date. This funding technique is interest neutral.

6.2.4 The following are terms under which State unique funding techniques shall be implemented for all transfers of funds to which the funding technique is applied in section 6.3.2 of this Agreement.

Modified Direct Program Costs -Admin, Payroll, Payments to Providers (ACH Drawdown on Payroll Cycle)

The State shall request funds for all direct administrative costs and/or payroll costs, and/or payments made to providers and to support providers. The request shall be made in accordance with the appropriate Federal agency cut-off time specified in Exhibit I. The amount of the funds requested shall be based on the amount of expenditures recorded for direct administrative costs and/or payroll costs and/or payments made to providers or to support providers since the last request for funds. The State payroll cycle is payday twice a month. Draws made day before payday are for deposit on payday. The draw request will be made in accordance with cut-off time in Exhibit 1. The amount of the funds requested shall be based on the amount of expenditures recorded for direct administrative costs and/or payroll costs and/or payments made

to providers or to support providers since the last request for funds. This funding technique is interest neutral.

6.3.2 Programs

10.557 Special Supplemental Nutrition Program for Women, Infants, and Children

Recipient: 303---Department of Health---DOH

% of Funds Agency Receives: 66.00

Component: Direct program/benefit payments for food voucher redemption through United Community Bank, which acts as the state's fiscal agent in the program. The state's drawdowns are based on the actual expenditures, which are the previous day's activity. Rebates offset the direct program/benefit payments. This is a zero balance account.

Technique: Actual Clearance, ZBA-ACH

Average Day of Clearance: 0 Days

Recipient: 303---Department of Health---DOH

% of Funds Agency Receives: 34.00

Component: Administrative costs including payroll

Technique: Modified Direct Program Costs -Admin, Payroll, Payments to Providers (ACH Drawdown on Payroll Cycle)

Average Day of Clearance: 0 Days

2018-007

The Office of the State Treasurer did not have adequate internal controls to properly identify and notify participating counties of the amount and source of funds they received for the Schools and Roads program.

Federal Awarding Agency: Department of Agriculture
Pass-Through Entity: None
CFDA Number and Title: 10.665 Schools and Roads – Grants to States
Federal Award Number: N/A
Applicable Compliance Component: Activities Allowed or Unallowed/Cost Principles
Known Questioned Cost Amount: None

Background

The Department of Agriculture (Department) shares federal receipts from the national forests with the states in which the national forests are situated. Federal Title I funds are generally to be used for the benefit of public schools and public roads of the county or counties in which the national forest is situated. Federal Title III portion of the funds are paid to participating counties to carry out activities under the Firewise Communities program, reimburse for search and rescue or other emergency services, or develop community wildfire protection plans.

The Office of the State Treasurer (Office) is responsible for transferring these federal funds for Washington to eligible counties. The Department sends the Office the program funds along with instructions on which counties are to receive the funds and how much and what type of funds each county is to receive. The Office is expected to disburse the Title I and any Title III funds according to the Department's instructions.

Description of Condition

The Office did not have adequate internal controls to properly identify and notify participating counties of the amount of Title III funds they received.

In May 2018, 14 counties received a total of \$667,658 in Title III funds from the Office. These funds should have been identified as Title III when given to the counties, but were identified as Title I. The Office detected the error after the audit period ended, while responding to a public records request, and corrected it at that time. The error was not detected as part of management's internal controls.

We consider this internal control deficiency to be a significant deficiency.

This condition was not reported in the prior audit.

Cause of Condition

The Office said the error occurred because of the infrequency of this program's funding to the State and staff lacked experience with this specific transaction. Additionally, management did not monitor sufficiently to ensure the grant funds were properly disbursed.

Effect of Condition

Title III funding is more restricted and has different allowable uses than Title I funds. The 14 counties were at risk for improperly spending these funds because the funding source was not correctly identified by the Office.

Recommendation

We recommend the Office:

- Ensure staff responsible for disbursing the funds are knowledgeable and aware of the different funding types
- Establish an adequate review of the disbursements to ensure the amounts and funding types are reported accurately to the counties

Office's Response

The Office of the State Treasurer (OST) is proud of its long history of clean audits and continual efforts to improve internal controls. However, OST respectfully disagrees with this audit finding. Upon learning the funding source was not correctly identified to the counties, OST notified the affected counties and sent corrected instructions for the federal grants distributed. This occurred within 60 days from the date of the error (May 22, 2018) and before the audit. Furthermore, OST followed up with each county and confirmed that funds were properly identified per federal instructions.

Within the Effect of Condition section, the State Auditor's Office (SAO) states that "... counties were at risk for improperly spending these funds ...". Due to OST's timely response and proactive communication, the chance of noncompliance by the counties occurring is slight (i.e., remote) at best. The impacted counties would have had to spend over 96 percent of the total money distributed by July 20, 2018 to inadvertently spend Title III funds on Title I purposes. Furthermore, this mistake was identified and corrected before the audit began.

According to SAO's "Decision Matrix for Single Audit Internal Control Deficiencies", if the likelihood of noncompliance is considered "Remote", then the control deficiency should not be considered significant. As such, deficiencies that are not significant do not require the SAO to report an audit finding.

OST considers this internal control deficiency to be not significant given the circumstances. OST does, however, appreciate the audit recommendations as they are internal control improvements. OST will continue to always enhance internal controls. In fact, in the last calendar year, an internal auditor position has been added to our staff. Although not required, the Treasurer and Treasury Management

decided that it was an important position to ensure financial integrity of public funds. This addresses the well-received recommendations for improvement provided in the Auditor's report.

Auditor's Concluding Remarks

The Office of the State Treasurer is correct that it identified the error prior to the audit being conducted. However, the identification did not occur before the end of the audit period and, most importantly, the error was not identified through the normal course of business. In its response, the Office asserts that the likelihood of noncompliance is remote. In fact, the Department became noncompliant when it mis-categorized the funds and dispersed them to the counties. Therefore, the likelihood of noncompliance is not remote.

In our judgement, the deficiency was not significant enough to report as a material weakness, but important enough to merit attention by agency management and the grantor.

We reaffirm our finding and will review the status of the Office's corrective action during our next audit.

Applicable Laws and Regulations

Title 2 U.S. Code of Federal Regulations Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance) establishes the following applicable requirements:

Section 200.302 Financial management, states:

- (a) Each state must expend and account for the Federal award in accordance with state laws and procedures for expending and accounting for the state's own funds. In addition, the state's and the other non-Federal entity's financial management systems, including records documenting compliance with Federal statutes, regulations, and the terms and conditions of the Federal award, must be sufficient to permit the preparation of reports required by general and program-specific terms and conditions; and the tracing of funds to a level of expenditures adequate to establish that such funds have been used according to the Federal statutes, regulations, and the terms and conditions of the Federal award. See also § 200.450 Lobbying.
- (b) The financial management system of each non-Federal entity must provide for the following (see also §§ 200.333 Retention requirements for records, 200.334 Requests for transfer of records, 200.335 Methods for collection, transmission and storage of information, 200.336 Access to records, and 200.337 Restrictions on public access to records):
 - (1) Identification, in its accounts, of all Federal awards received and expended and the Federal programs under which they were received. Federal program and Federal award identification must include, as applicable, the CFDA title and number, Federal award identification number and year, name of the Federal agency, and name of the pass-through entity, if any.

- (2) Accurate, current, and complete disclosure of the financial results of each Federal award or program in accordance with the reporting requirements set forth in §§ 200.327 Financial reporting and 200.328 Monitoring and reporting program performance. If a Federal awarding agency requires reporting on an accrual basis from a recipient that maintains its records on other than an accrual basis, the recipient must not be required to establish an accrual accounting system. This recipient may develop accrual data for its reports on the basis of an analysis of the documentation on hand. Similarly, a pass-through entity must not require a subrecipient to establish an accrual accounting system and must allow the subrecipient to develop accrual data for its reports on the basis of an analysis of the documentation on hand.
- (3) Records that identify adequately the source and application of funds for federally funded activities. These records must contain information pertaining to Federal awards, authorizations, obligations, unobligated balances, assets, expenditures, income and interest and be supported by source documentation.
- (4) Effective control over, and accountability for, all funds, property, and other assets. The non-Federal entity must adequately safeguard all assets and assure that they are used solely for authorized purposes. See § 200.303 Internal controls.
- (5) Comparison of expenditures with budget amounts for each Federal award.
- (6) Written procedures to implement the requirements of § 200.305 Payment.
- (7) Written procedures for determining the allowability of costs in accordance with Subpart E—Cost Principles of this part and the terms and conditions of the Federal award.

Section 200.303 Internal controls, states in part:

The non-Federal entity must:

- (a) Establish and maintain effective internal control over the Federal award that provides reasonable assurance that the non-Federal entity is managing the Federal award in compliance with Federal statutes, regulations, and the terms and conditions of the Federal award. These internal controls should be in compliance with guidance in “Standards for Internal Control in the Federal Government” issued by the Comptroller General of the United States or the “Internal Control Integrated Framework”, issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).

Section 200.516 Audit findings, states in part:

- (a) *Audit findings reported.* The auditor must report the following as audit findings in a schedule of findings and questioned costs:
 - (1) Significant deficiencies and material weaknesses in internal control over major programs and significant instances of abuse relating to major programs. The auditor’s determination of whether a deficiency in internal control is a significant deficiency or material weakness for the purpose of reporting an audit finding is in relation to a type of compliance requirement for a major program identified in the Compliance Supplement.

The American Institute of Certified Public Accountants defines significant deficiencies and material weaknesses in internal controls over compliance in its *Codification of Statements on Auditing Standards*, section 935, Compliance Audits, as follows:

.11 For purposes of adapting GAAS to a compliance audit, the following terms have the meanings attributed as follows: ...

Deficiency in internal control over compliance. A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance on a timely basis. A deficiency in design exists when (a) a control necessary to meet the control objective is missing, or (b) an existing control is not properly designed so that, even if the control operates as designed, the control objective would not be met. A deficiency in operation exists when a properly designed control does not operate as designed or the person performing the control does not possess the necessary authority or competence to perform the control effectively.

Material weakness in internal control over compliance. A deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a compliance requirement will not be prevented, or detected and corrected, on a timely basis. In this section, a reasonable possibility exists when the likelihood of an event occurring is either reasonably possible or probable as defined as follows:

Reasonably possible. The chance of the future event or events occurring is more than remote but less than likely.

Probable. The future event or events are likely to occur.

Significant deficiency in internal control over compliance. A deficiency, or a combination of deficiencies, in internal control over compliance that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

2018-008 The Military Department charged payroll costs to the Military Operations and Maintenance program that were not properly supported.

Federal Awarding Agency: National Guard Bureau
Pass-Through Entity: None
CFDA Number and Title: 12.401 National Guard Military Operations and Maintenance
Federal Award Number: W912K3-15-2-1000
Applicable Compliance Component: Activities Allowed or Unallowed Allowable Cost/Cost Principles
Known Questioned Cost Amount: \$82,338

Background

The Washington State Military Department (Department) administers the National Guard Military Operations and Maintenance Projects. The National Guard Bureau (NGB) and the Department enter into a Master Cooperative Agreement to establish the terms and conditions applicable to the contribution of NGB funds or in-kind assistance for the operation and training of the Washington State Army and Air National Guard.

The Department can use grant funds only for costs that are allowable and related to the grant’s purpose. According to Department policy, employees whose positions are funded by a single federal award or a single cost activity must complete a certification stating they have worked solely on the specific federal program. The certification must be reviewed for accuracy and approved by the employee’s supervisor by the last day of the following month for the quarter. Employees who work on additional cost activities, other than the grant program, must complete a timesheet twice a month.

In fiscal year 2018, the Department received about \$21.3 million in federal funds for the operations and maintenance of the Army National Guard and Air National Guard facilities. Of this amount, over \$7.9 million was spent on employee salaries and benefits.

Description of Condition

The Military Department charged payroll costs to the Military Operations and Maintenance program that were not properly supported.

Nine employees were required to submit certifications quarterly. We reviewed all 36 certifications, which were completed for work performed during the audit period, and found seven were submitted as many as 139 days late. Three certifications were eventually collected during the audit period, but four were not collected by the last day of the month following the end of the state fiscal year.

This condition was not reported in the prior audit.

Cause of Condition

The Department had policies in place to ensure compliance, but they were not always followed. Management followed up with each employee and their supervisor when the certifications were not submitted in a timely manner, but could not obtain the certifications.

Effect of Condition and Questioned Costs

The Department charged \$82,338 in direct payroll and benefits to the program that were not adequately supported. We are questioning these costs.

We question costs when we find an agency has not complied with grant requirements or when it does not have adequate documentation to support its expenditures.

Recommendation

We recommend the Department:

- Follow its own policy to ensure payroll costs charged to a federal grant are supported by required documentation
- Consult with the grantor to discuss whether the questioned costs identified in the audit should be repaid

Department's Response

The Department concurs with the findings.

The Department policy requires employees who are permanently assigned to activities directly benefiting a single federal program to submit a Certification of Time and Effort on a quarterly basis. Supervisors are required by policy to review for accuracy and submit the form to the Payroll Office. In some cases, despite the Payroll Office sending reminders to employees and their supervisors, the Certification of Time and Effort forms were never submitted to the Payroll Office.

The Department will initiate the following actions:

- *Update the "Time and Effort Reporting Certification" policy and "Time and Effort Reporting" policy to ensure timekeeping guidance and requirements are clear and understood.*
- *Provide copies of the policy to employee and supervisor who are permanently assigned to activities directly benefiting a single federal program and are not overtime eligible.*
- *Train employees and supervisors of the importance of the procedure.*
- *Implement a quarterly monitoring task for employees and supervisor.*
- *If Certification forms are not received by due date established in the Department policies, Payroll Office will follow up with the supervisor and escalate as necessary until required documentation is received.*

Auditor's Concluding Remarks

We thank the Department for its cooperation and assistance throughout the audit. We will review the status of the Department's corrective action during our next audit.

Applicable Laws and Regulations

Title 2 U.S. Code of Federal Regulations Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance) establishes the following applicable requirements:

Section 200.53 Improper Payments states:

- (a) *Improper payment* means any payment that should not have been made or that was made in an incorrect amount (including overpayments and underpayments) under statutory, contractual, administrative, or other legally applicable requirements; and
- (b) *Improper payment* includes any payment to an ineligible party, any payment for an ineligible good or service, any duplicate payment, any payment for a good or service not received (except for such payments where authorized by law), any payment that does not account for credit for applicable discounts, and any payment where insufficient or lack of documentation prevents a reviewer from discerning whether a payment was proper.

Section 200.403 Factors affecting Allowability of costs.

Except where otherwise authorized by statute, costs must meet the following general criteria in order to be allowable under Federal awards.

- (a) Be necessary and reasonable for the performance of the Federal award and be allocable thereto under these principles.
- (b) Conform to any limitations or exclusions set forth in these principles or in the Federal award as to types or amount of cost items.
- (c) Be consistent with policies and procedures that apply uniformly to both federally-financed and other activities of the non-Federal entity.
- (d) Be accorded consistent treatment. A cost may not be assigned to a Federal award as a direct cost if any other cost incurred for the same purpose in like circumstances has been allocated to the Federal award as an indirect cost.
- (e) Be determined in accordance with generally accepted accounting principles (GAAP), except, for state and local governments and Indian tribes only, as otherwise provided for in this part.
- (f) Not be included as a cost or used to meet cost sharing or matching requirements of any other federally-financed program in either the current or a prior period. See also §200.306 Cost sharing or matching paragraph (b).
- (g) Be adequately documented. See also §§200.300 Statutory and national policy requirements through 200.309 Period of performance of this part.

Section 200.410 Collection of unallowable costs.

Payments made for costs determined to be unallowable by either the Federal awarding agency, cognizant agency for indirect costs, or pass-through entity, either as direct or indirect costs, must be refunded (including interest) to the Federal Government in accordance with instructions from the Federal agency that determined the costs are unallowable unless Federal statute or regulation directs otherwise. See also Subpart D— Post Federal Award Requirements of this part, §§200.300 Statutory and national policy requirements through 200.309 Period of performance.

Section 200.516 Audit findings, states in part:

(a) *Audit findings reported.* The auditor must report the following as audit findings in a schedule of findings and questioned costs:

- (3) Known questioned costs that are greater than \$25,000 for a type of compliance requirement for a major program. Known questioned costs are those specifically identified by the auditor. In evaluating the effect of questioned costs on the opinion on compliance, the auditor considers the best estimate of total costs questioned (likely questioned costs), not just the questioned costs specifically identified (known questioned costs). The auditor must also report known questioned costs when likely questioned costs are greater than \$25,000 for a type of compliance requirement for a major program. In reporting questioned costs, the auditor must include information to provide proper perspective for judging the prevalence and consequences of the questioned costs.

The Military Department, Finance Division Procedure 02-005A-06, states in part:

Certification Requirements apply to employees that are permanently assigned to activities directly benefiting a single federal program. Quarterly, these employees must complete a Certification of Time and Effort form (MIL Form 806) that certifies the employee worked solely on a specified federal program for the specified period of time. The employee completes the certification of time and effort. Employee submits the certification to their designated supervisor. Supervisor reviews the certificate for accuracy, then signs and dates if accurate and complete. Supervisors must ensure that certifications are submitted to the payroll staff by the last day of the following month.

2018-009

The Office of Civil Legal Aid did not have adequate internal controls over and did not comply with federal requirements to ensure subrecipients of the Crime Victim Assistance program received required audits.

Federal Awarding Agency: Department of Justice
Pass-Through Entity: None
CFDA Number and Title: 16.575 Crime Victim Assistance
Federal Award Number: 2015-VA-GX-0031
2016-VA-GX-0044
Applicable Compliance Component: Subrecipient Monitoring
Known Questioned Cost Amount: None

Background

The Office of Civil Legal Aid (Office) receives federal funding for Crime Victim Assistance through an interlocal agreement with the Department of Commerce. It subsequently subawards federal funds to seven nonprofit subrecipients to provide legal advice, assistance and representation to victims of crime in Washington. Each nonprofit is funded under its own subrecipient contract. The Office spent \$4.6 million in federal funds for Crime Victim Assistance in state fiscal year 2018. Of that amount, about \$4.4 million was passed through to subrecipients as subawards.

Federal regulations require the Office to monitor the activities of its subrecipients. This includes verifying that its subrecipients that spend \$750,000 or more in federal awards during a fiscal year obtain a single audit. Further, for the awards it passes on to its subrecipients, the Office must follow up and ensure its subrecipients take timely action on all deficiencies detected through audits, onsite reviews and other means, and must issue a management decision for audit findings within six months of the audit report's acceptance by the Federal Audit Clearinghouse. These requirements help ensure grant money is used for authorized purposes and within the provisions of contracts or grant agreements.

Description of Condition

The Office did not have adequate internal controls over and did not comply with federal requirements to ensure subrecipients of the Crime Victim Assistance program received required audits. During the subaward process, subrecipients are notified of the requirement to submit all single audit reports timely once completed. However, management said the Office does not track when audits are due or confirm that they were either performed or not required. Management also said that of the seven subrecipients, it expects only two will meet the \$750,000 required threshold for needing to obtain and submit an audit and they are expected to provide those audits to the Office.

We found the Office did not have adequate internal controls in place to verify:

- Subrecipients received required audits
- Findings were followed up on and management decisions were issued when due

We found six of the seven subrecipients of the Crime Victim Assistance program were not monitored to ensure their compliance with requirements for obtaining single audits. Of these six, two required an audit. We reviewed the two audits that were not collected and determined one subrecipient received an audit finding related to the program that included questioned costs. The Office was required to issue a management decision to the subrecipient for this finding and ensure the issue was corrected. Because it was not aware of this finding, the Office did not perform the required follow-up.

We consider these internal control weaknesses to constitute a material weakness.

This condition was not reported in the prior audit.

Cause of Condition

The Office did not establish policies or procedures to verify whether each subrecipient required a single audit, monitor audit results, or ensure it issued timely management decisions when required.

Effect of Condition

Without establishing adequate internal controls, the Office cannot ensure all subrecipients that met the threshold for an audit complied with federal grant requirements. In addition, one subrecipient never received a management decision for one of its findings.

Recommendations

We recommend the Office:

- Establish policies and procedures related to subrecipient audit monitoring
- Verify all required audits occurred
- Follow up on subrecipient audit findings related to the program and issue a management decision promptly

Office's Response

The Office of Civil Legal Aid has received this audit finding. We concur with both the finding and SAO's recommendations. Effective January 31, 2019, action was taken to: (a) establish appropriate policies and procedures to ensure subrecipient audit monitoring and review, and (b) review and follow up on audit findings, if any, for those subrecipients that are subject to the Single Audit requirement and have received audit findings.

Auditor's Concluding Remarks

We thank the Office for its cooperation and assistance throughout the audit. We will review the status of the Office's corrective action during our next audit.

Applicable Laws and Regulations

Title 2 U.S. Code of Federal Regulations Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance) establishes the following applicable requirements:

Section 200.303 Internal controls, states in part:

The non-Federal entity must:

- (a) Establish and maintain effective internal control over the Federal award that provides reasonable assurance that the non-Federal entity is managing the Federal award in compliance with Federal statutes, regulations, and the terms and conditions of the Federal award. These internal controls should be in compliance with guidance in “Standards for Internal Control in the Federal Government” issued by the Comptroller General of the United States or the “Internal Control Integrated Framework”, issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).
- (b) Comply with Federal statutes, regulations, and the terms and conditions of the Federal awards.
- (d) Take prompt action when instances of noncompliance are identified including noncompliance identified in audit findings.

Section 200.516 Audit findings, states in part:

- (a) *Audit findings reported.* The auditor must report the following as audit findings in a schedule of findings and questioned costs:
 - (1) Significant deficiencies and material weaknesses in internal control over major programs and significant instances of abuse relating to major programs. The auditor’s determination of whether a deficiency in internal control is a significant deficiency or material weakness for the purpose of reporting an audit finding is in relation to a type of compliance requirement for a major program identified in the Compliance Supplement.
 - (2) Material noncompliance with the provisions of Federal statutes, regulations, or the terms and conditions of Federal awards related to a major program. The auditor’s determination of whether a noncompliance with the provisions of Federal statutes, regulations, or the terms and conditions of Federal awards is material for the purpose of reporting an audit finding is in relation to a type of compliance requirement for a major program identified in the compliance supplement.

Section 200.331 Requirements for pass-through entities, states in part:

All pass-through entities must:

- (d) Monitor the activities of the subrecipient as necessary to ensure that the subaward is used for authorized purposes, in compliance with Federal statutes, regulations, and the terms and conditions of the subaward; and that subaward performance goals are achieved. Pass-through entity monitoring of the subrecipient must include:
 - (1) Reviewing financial and performance reports required by the pass-through entity.
 - (2) Following-up and ensuring that the subrecipient takes timely and appropriate action on all deficiencies pertaining to the Federal award provided to the subrecipient from the pass-through entity detected through audits, on-site reviews, and other means.

- (3) Issuing a management decision for audit findings pertaining to the Federal award provided to the subrecipient from the pass-through entity as required by §200.521 Management decision.
- (f) Verify that every subrecipient is audited as required by Subpart F—Audit Requirements of this part when it is expected that the subrecipient's Federal awards expended during the respective fiscal year equaled or exceeded the threshold set forth in §200.501 Audit requirements.

The American Institute of Certified Public Accountants defines significant deficiencies and material weaknesses in internal controls over compliance in its *Codification of Statements on Auditing Standards*, section 935, Compliance Audits, as follows:

.11 For purposes of adapting GAAS to a compliance audit, the following terms have the meanings attributed as follows: ...

Deficiency in internal control over compliance. A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance on a timely basis. A deficiency in design exists when (a) a control necessary to meet the control objective is missing, or (b) an existing control is not properly designed so that, even if the control operates as designed, the control objective would not be met. A deficiency in operation exists when a properly designed control does not operate as designed or the person performing the control does not possess the necessary authority or competence to perform the control effectively.

Material weakness in internal control over compliance. A deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a compliance requirement will not be prevented, or detected and corrected, on a timely basis. In this section, a reasonable possibility exists when the likelihood of an event occurring is either reasonably possible or probable as defined as follows:

Reasonably possible. The chance of the future event or events occurring is more than remote but less than likely.

Probable. The future event or events are likely to occur.

Significant deficiency in internal control over compliance. A deficiency, or a combination of deficiencies, in internal control over compliance that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

Material noncompliance. In the absence of a definition of material noncompliance in the governmental audit requirement, a failure to follow compliance requirements or a violation of prohibitions included in the applicable compliance requirements that results in noncompliance that is quantitatively or qualitatively material, either individually or when aggregated with other noncompliance, to the affected government program.

2018-010

The Office of Civil Legal Aid did not have adequate internal controls over and did not comply with requirements to ensure subrecipients of the Crime Victim Assistance Program received required risk assessments.

Federal Awarding Agency: Department of Justice
Pass-Through Entity: None
CFDA Number and Title: 16.575 Crime Victim Assistance
Federal Award Number: 2015-VA-GX-0031
2016-VA-GX-0044
Applicable Compliance Component: Subrecipient Monitoring
Known Questioned Cost Amount: None

Background

The Office of Civil Legal Aid (Office) receives federal funding for Crime Victim Assistance through an interlocal agreement from the Department of Commerce. It subsequently subawards federal funds to seven nonprofit subrecipients to provide legal advice, assistance and representation to victims of crime in Washington. Each nonprofit is funded under its own subrecipient contract. The Office spent \$4.6 million in federal funds for Crime Victim Assistance in state fiscal year 2018. Of that amount, about \$4.4 million was passed through to seven subrecipients as subawards.

To determine the appropriate level of monitoring, federal regulations require the Office to evaluate each subrecipient's risk of noncompliance with federal statutes, regulations, and the terms and conditions of the subaward.

Description of Condition

The Office did not have adequate internal controls over and did not comply with requirements to ensure subrecipients received required risk assessments for the Crime Victim Assistance Program.

While the Office had procedures for performing subrecipient monitoring, it did not require staff to perform a risk assessment of each subrecipient to determine the appropriate level of monitoring as required by federal regulations. Subsequently, no risk assessments were performed for any of the Office's seven subrecipients.

We consider this internal control deficiency to be a material weakness.

This condition was not reported in the prior audit.

Cause of Condition

The Office had no policies or procedures in place that address how risk assessments of subrecipients should be performed and documented. Management said they thought the Office was already meeting the requirement through its onsite monitoring process.

Effect of Condition

By not performing risk assessments of subrecipients, the Office is less likely to perform adequate monitoring that would detect whether subrecipients comply with grant terms and federal regulations. Without written policies and procedures, the Office cannot ensure risk assessments are performed consistently and analyze the proper criteria, which would ensure consistency in determining the appropriate amount of monitoring for each subrecipient.

Recommendations

We recommend the Office:

- Establish adequate internal controls, including policies and procedures, to ensure required risk assessments are performed
- Maintain documentation to show the required risk assessments were performed, which would allow management to monitor the results and demonstrate compliance with federal requirements
- Ensure the results of the risk assessments are used to determine how much and what type of monitoring of subrecipients will be performed, as required by federal law

Office's Response

The Office of Civil Legal Aid has received this audit finding. We concur with both the finding and SAO's recommendations. Effective January 31, 2019, action was taken to increase internal controls by adopting a formal risk assessment protocol, developing and employing a risk assessment tool, and adopting a risk assessment schedule that will allow timely assessment of and action necessary to mitigate any risks associated with existing and future proposed subrecipients of federal VOCA funding.

Auditor's Concluding Remarks

We thank the Office for its cooperation and assistance throughout the audit. We will review the status of the Office's corrective action during our next audit.

Applicable Laws and Regulations

Title 2 U.S. Code of Federal Regulations Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance) establishes the following applicable requirements:

Section 200.303 Internal controls, states in part:

The non-Federal entity must:

- (a) Establish and maintain effective internal control over the Federal award that provides reasonable assurance that the non-Federal entity is managing the Federal award in compliance with Federal statutes, regulations, and the terms and conditions of the Federal award. These internal controls should be in compliance with guidance in

“Standards for Internal Control in the Federal Government” issued by the Comptroller General of the United States or the “Internal Control Integrated Framework”, issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).

- (b) Comply with Federal statutes, regulations, and the terms and conditions of the Federal awards.
- (d) Take prompt action when instances of noncompliance are identified including noncompliance identified in audit findings.

Section 200.516 Audit findings, states in part:

- (a) *Audit findings reported.* The auditor must report the following as audit findings in a schedule of findings and questioned costs:
 - (1) Significant deficiencies and material weaknesses in internal control over major programs and significant instances of abuse relating to major programs. The auditor’s determination of whether a deficiency in internal control is a significant deficiency or material weakness for the purpose of reporting an audit finding is in relation to a type of compliance requirement for a major program identified in the Compliance Supplement.
 - (2) Material noncompliance with the provisions of Federal statutes, regulations, or the terms and conditions of Federal awards related to a major program. The auditor’s determination of whether a noncompliance with the provisions of Federal statutes, regulations, or the terms and conditions of Federal awards is material for the purpose of reporting an audit finding is in relation to a type of compliance requirement for a major program identified in the compliance supplement.

Section 200.331 Requirements for pass-through entities, states in part:

All pass-through entities must:

- (b) Evaluate each subrecipient's risk of noncompliance with Federal statutes, regulations, and the terms and conditions of the subaward for purposes of determining the appropriate subrecipient monitoring described in paragraphs (d) and (e) of this section, which may include consideration of such factors as:
 - (1) The subrecipient's prior experience with the same or similar subawards;
 - (2) The results of previous audits including whether or not the subrecipient receives a Single Audit in accordance with Subpart F—Audit Requirements of this part, and the extent to which the same or similar subaward has been audited as a major program;
 - (3) Whether the subrecipient has new personnel or new or substantially changed systems; and
 - (4) The extent and results of Federal awarding agency monitoring (e.g., if the subrecipient also receives Federal awards directly from a Federal awarding agency).

The American Institute of Certified Public Accountants defines significant deficiencies and material weaknesses in internal controls over compliance in its *Codification of Statements on Auditing Standards*, section 935, Compliance Audits, as follows:

.11 For purposes of adapting GAAS to a compliance audit, the following terms have the meanings attributed as follows: ...

Deficiency in internal control over compliance. A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow

management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance on a timely basis. A deficiency in design exists when (a) a control necessary to meet the control objective is missing, or (b) an existing control is not properly designed so that, even if the control operates as designed, the control objective would not be met. A deficiency in operation exists when a properly designed control does not operate as designed or the person performing the control does not possess the necessary authority or competence to perform the control effectively.

Material weakness in internal control over compliance. A deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a compliance requirement will not be prevented, or detected and corrected, on a timely basis. In this section, a reasonable possibility exists when the likelihood of an event occurring is either reasonably possible or probable as defined as follows:

Reasonably possible. The chance of the future event or events occurring is more than remote but less than likely.

Probable. The future event or events are likely to occur.

Significant deficiency in internal control over compliance. A deficiency, or a combination of deficiencies, in internal control over compliance that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

Material noncompliance. In the absence of a definition of material noncompliance in the governmental audit requirement, a failure to follow compliance requirements or a violation of prohibitions included in the applicable compliance requirements that results in noncompliance that is quantitatively or qualitatively material, either individually or when aggregated with other noncompliance, to the affected government program.

Office of Management and Budget's Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards 2 CFR 200 – Frequently Asked Questions

.331-10 Requirements for Pass-Through Entities. Timing of Subrecipient Risk Assessments, states in part:

Section §200.331 (b) indicates that pass-through entities must “evaluate each subrecipient’s risk of noncompliance with Federal statutes, regulations, and the terms and conditions of the subaward for purposes of determining the appropriate subrecipient monitoring...” Are pass-through entities required to assess the risk of non-compliance for each applicant prior to issuing a subaward?

No. While section §200.331 (b) requires risk assessments of subrecipients, there is no requirement for pass-through entities to perform these assessments before making subawards. Under the Uniform Guidance, the purpose of these risk assessments is for pass-through entities to determine appropriate subrecipient monitoring. Pass-through entities may use judgment regarding the most appropriate timing for the assessments. Regardless of the timing chosen, the pass-through entity should document its procedures for assessing risk. Section §200.331 (b) (1)– (4) includes factors that a pass-through entity may consider when assessing subrecipient risk.

Additionally, the regulation referenced by the Department is not the one containing the requirements for suspension and debarment.

Effect of Condition

Without a clause or condition in its agreements, the Department risks not identifying a suspended or debarred subrecipient before issuing it an award. If payments were made to subrecipients who were suspended or debarred, the payments would be unallowable and the Department might have to repay the grantor.

Recommendations

We recommend the Department establish and implement adequate internal controls to ensure a suspension and debarment clause or condition is included in all local agency agreements.

Department's Response

We appreciate the State Auditor's Office (SAO) audit of the Federal Highway Program. WSDOT is committed to ensuring our programs comply with federal regulations. We understand it is SAO's point of view that the Department did not have adequate contract language in place to verify that Local Agencies were not suspended or debarred. We are in the process of updating our Local Agency Manual to include an appropriate clause so that Local Agencies certify that they are not suspended or debarred.

The risk that any of the Local Agencies that receive federal awards from WSDOT are suspended or debarred is very low. WSDOT Local Programs staff determined that none of the Local Agencies that received payments for FY 2018 were either suspended or debarred.

Auditor's Concluding Remarks

We thank the Department for its cooperation and assistance throughout the audit. We will review the status of the Department's corrective action during our next audit.

Applicable Laws and Regulations

Title 2 U.S. Code of Federal Regulations Part 200, Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards (Uniform Guidance) establishes the following applicable requirements.

Section 200.303 Internal controls. The non-Federal entity must:

- (a) Establish and maintain effective internal control over the Federal award that provides reasonable assurance that the non-Federal entity is managing the Federal award in compliance with Federal statutes, regulations, and the terms and conditions of the Federal award. These internal controls should be in compliance with guidance in "Standards for Internal Control in the Federal Government" issued by the Comptroller General of the United States or the "Internal Control Integrated

Framework”, issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).

- (b) Comply with Federal statutes, regulations, and the terms and conditions of the Federal awards.
- (d) Take prompt action when instances of noncompliance are identified including noncompliance identified in audit findings.

Section 200.516 Audit reporting, states in part:

- (a) Audit findings reported. The auditor must report the following as audit findings in a schedule of findings and questioned costs:

(1) Significant deficiencies and material weaknesses in internal control over major programs and significant instances of abuse relating to major programs. The auditor’s determination of whether a deficiency in internal control is a significant deficiency or material weakness for the purpose of reporting an audit finding is in relation to a type of compliance requirement for a major program identified in the Compliance Supplement.

(2) Material noncompliance with the provisions of Federal statutes, regulations, or the terms and conditions of Federal awards related to a major program. The auditor’s determination of whether a noncompliance with the provisions of Federal statutes, regulations, or the terms and conditions of Federal awards is material for the purpose of reporting an audit finding is in relation to a type of compliance requirement for a major program identified in the compliance supplement.

The American Institute of Certified Public Accountants defines significant deficiencies and material weaknesses in internal controls over compliance in its Codification of Statements on Auditing Standards, section 935, Compliance Audits, as follows:

11. For purposes of adapting GAAS to a compliance audit, the following terms have the meanings attributed as follows: ...

Deficiency in internal control over compliance. A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance on a timely basis. A deficiency in design exists when (a) a control necessary to meet the control objective is missing, or (b) an existing control is not properly designed so that, even if the control operates as designed, the control objective would not be met. A deficiency in operation exists when a properly designed control does not operate as designed or the person performing the control does not possess the necessary authority or competence to perform the control effectively.

Material weakness in internal control over compliance. A deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a compliance requirement will not be prevented, or detected and

corrected, on a timely basis. In this section, a reasonable possibility exists when the likelihood of an event occurring is either reasonably possible or probable as defined as follows:

Reasonably possible. The chance of the future event or events occurring is more than remote but less than likely.

Probable. The future event or events are likely to occur.

Significant deficiency in internal control over compliance. A deficiency, or a combination of deficiencies, in internal control over compliance that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

Material noncompliance. In the absence of a definition of material noncompliance in the governmental audit requirement, a failure to follow compliance requirements or a violation of prohibitions included in the applicable compliance requirements that results in noncompliance that is quantitatively or qualitatively material, either individually or when aggregated with other noncompliance, to the affected government program.

Title 2, U.S. Code of Federal Regulation, part 1200.332, Department of Transportation Nonprocurement Suspension and Debarment: states in part:

What methods must I use to pass requirements down to participants at lower tiers with whom I intend to do business?

You as a participant must include a term or condition in lower-tier transactions requiring lower tier participants to comply with subpart C of the OMB guidance in 2 CFR part 180, as supplemented by this subpart.

Title 2, U.S. Code of Federal Regulation, part 180, states in part:

Subpart B – Covered Transactions

A covered transactions is a nonprocurement or procurement transactions that is subject to the prohibitions of this part. It may be a transaction at –

(a) The primary tier, between a Federal agency and a person (see appendix to this part);

or

(b) A lower tier, between a participant in a covered transaction and another person.

Subpart C–Responsibilities of Participants Regarding Transactions Doing Business With Other Persons

§180.300 What must I do before I enter into a covered transaction with another person at the next lower tier?

When you enter into a covered transaction with another person at the next lower tier, you must verify that the person with whom you intend to do business is not excluded or disqualified. You do this by:

(a) Checking SAM Exclusions; or

(b) Collecting a certification from that person; or

(c) Adding a clause or condition to the covered transaction with that person

2018-012 **The Department of Transportation did not have adequate internal controls over and did not comply with requirements to perform risk assessments for subrecipients of the Highway Planning and Construction Cluster.**

Federal Awarding Agency: U.S. Department of Transportation
Pass-Through Entity: None
CFDA Number and Title: 20.205 Highway Planning and Construction Cluster
20.219
20.224
Federal Award Number: Too numerous to list. All approved subaward projects under the Stewardship and Oversight Agreement
Applicable Compliance Component: Subrecipient Monitoring
Known Questioned Cost Amount: None

Background

The Washington Department of Transportation (DOT) Local Programs Office administers federal funding under the Highway Planning and Construction Cluster to local agencies throughout the state for highway construction projects. Cities, counties, ports, tribes, districts, councils and boards can all be considered local agencies. Every project is funded under its own subaward, called a local agency agreement. The Department spent about \$616 million in federal funds on highway projects during fiscal year 2018. Of that amount, \$199 million was passed through to local agencies as subawards.

To determine the appropriate level of monitoring, federal regulations require the Department to evaluate each subrecipient’s risk of noncompliance with federal statutes and regulations, and the terms and conditions of the subaward. During fiscal year 2018, the Department awarded about \$260 million in new subawards to 144 separate local agencies for over 400 highway construction projects across the state.

Staff in the Local Programs Office at DOT headquarters perform onsite monitoring of every local agency with an open and active project once every three years, and staff in the six regional offices perform a documentation review of each local agency in their respective regions annually.

Description of Condition

The Department did not have adequate internal controls over and did not comply with requirements to perform risk assessments for subrecipients of the Highway Planning and Construction Cluster.

The Department had no policies or procedures in place that address how risk assessments of subrecipients should be performed and documented. When the Department prepares to monitor or review an agency, it selects an open and active project and evaluates the agency based on its performance under that project. The Department had written procedures for performing subrecipient monitoring at both the regional and headquarters levels that directed staff to consider various factors

such as the complexity of the projects and past performance of the agency when determining which project to select. It did not, however, require staff to perform a risk assessment of the agency to determine the appropriate level of monitoring as required by federal regulations.

We consider this internal control deficiency to be a material weakness.

This condition was not reported in the prior audit.

Cause of Condition

Management did not ensure the Department met the federal requirement to perform risk assessments of subrecipients. Management at headquarters said they thought the Department was already meeting the requirement through its onsite monitoring process. Local Program Engineers in the six regions who were responsible for performing subrecipient monitoring said they considered various risk factors when determining which project to select for their documentation reviews, but were not aware of the federal requirement to perform risk assessments of subrecipients.

Effect of Condition

By not performing risk assessments of subrecipients, the Department is less likely to detect whether subrecipients comply with grant terms and federal regulations. Without written policies and procedures, the Department cannot ensure risk assessments are performed consistently and analyze the proper criteria, which would ensure consistency in determining the appropriate amount of monitoring for each subrecipient.

Recommendations

We recommend the Department establish and follow adequate internal controls to ensure required risk assessments are performed. Examples include:

- Establish policies and procedures that require staff to conduct risk assessments for all new subawards and provide criteria that staff should consider when they perform the assessments
- Maintain documentation to show the required risk assessments were performed, which would allow management to monitor the results and demonstrate compliance with federal requirements

Department's Response

We appreciate the State Auditor's Office (SAO) audit of the Federal Highway Program. WSDOT is committed to ensuring our programs comply with federal regulations and understand it is SAO's point of view documentation must be maintained in order to verify WSDOT's compliance with the requirement to assess risk to inform our monitoring of local agencies. We will work with the necessary parties to develop a system for documenting risk assessments of subrecipients which not only meet audit standards, but provides benefit to the agency.

Auditor’s Concluding Remarks

We thank the Department for its cooperation and assistance throughout the audit. We will review the status of the Department’s corrective action during our next audit.

Applicable Laws and Regulations

Title 2 U.S. Code of Federal Regulations Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance) establishes the following applicable requirements:

Section 200.303 Internal controls, states in part:

The non-Federal entity must:

- (a) Establish and maintain effective internal control over the Federal award that provides reasonable assurance that the non-Federal entity is managing the Federal award in compliance with Federal statutes, regulations, and the terms and conditions of the Federal award. These internal controls should be in compliance with guidance in “Standards for Internal Control in the Federal Government” issued by the Comptroller General of the United States or the “Internal Control Integrated Framework”, issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).
- (b) Comply with Federal statutes, regulations, and the terms and conditions of the Federal awards.
- (d) Take prompt action when instances of noncompliance are identified including noncompliance identified in audit findings.

Section 200.516 Audit findings, states in part:

- (a) *Audit findings reported.* The auditor must report the following as audit findings in a schedule of findings and questioned costs:
 - (1) Significant deficiencies and material weaknesses in internal control over major programs and significant instances of abuse relating to major programs. The auditor’s determination of whether a deficiency in internal control is a significant deficiency or material weakness for the purpose of reporting an audit finding is in relation to a type of compliance requirement for a major program identified in the Compliance Supplement.
 - (2) Material noncompliance with the provisions of Federal statutes, regulations, or the terms and conditions of Federal awards related to a major program. The auditor’s determination of whether a noncompliance with the provisions of Federal statutes, regulations, or the terms and conditions of Federal awards is material for the purpose of reporting an audit finding is in relation to a type of compliance requirement for a major program identified in the compliance supplement.

Section 200.331 Requirements for pass-through entities, states in part: All pass-through entities must:

- (b) Evaluate each subrecipient's risk of noncompliance with Federal statutes, regulations, and the terms and conditions of the subaward for purposes of determining the appropriate subrecipient monitoring described in paragraphs (d) and (e) of this section, which may include consideration of such factors as:
 - (1) The subrecipient's prior experience with the same or similar subawards;
 - (2) The results of previous audits including whether or not the subrecipient receives a Single Audit in accordance with Subpart F—Audit Requirements of this part, and the extent to which the same or similar subaward has been audited as a major program;
 - (3) Whether the subrecipient has new personnel or new or substantially changed systems; and
 - (4) The extent and results of Federal awarding agency monitoring (e.g., if the subrecipient also receives Federal awards directly from a Federal awarding agency).

The American Institute of Certified Public Accountants defines significant deficiencies and material weaknesses in internal controls over compliance in its *Codification of Statements on Auditing Standards*, section 935, Compliance Audits, as follows:

.11 For purposes of adapting GAAS to a compliance audit, the following terms have the meanings attributed as follows: ...

Deficiency in internal control over compliance. A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance on a timely basis. A deficiency in design exists when (a) a control necessary to meet the control objective is missing, or (b) an existing control is not properly designed so that, even if the control operates as designed, the control objective would not be met. A deficiency in operation exists when a properly designed control does not operate as designed or the person performing the control does not possess the necessary authority or competence to perform the control effectively.

Material weakness in internal control over compliance. A deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a compliance requirement will not be prevented, or detected and corrected, on a timely basis. In this section, a reasonable possibility exists when the likelihood of the event is either reasonably possible or probable as defined as follows:

Reasonably possible. The chance of the future event or events occurring is more than remote but less than likely.

Probable. The future event or events are likely to occur.

Significant deficiency in internal control over compliance. A deficiency, or a combination of deficiencies, in internal control over compliance that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

Material noncompliance. In the absence of a definition of material noncompliance in the governmental audit requirement, a failure to follow compliance requirements or a violation of prohibitions included in the applicable compliance requirements that results in noncompliance that is quantitatively or qualitatively material, either individually or when aggregated with other noncompliance, to the affected government program.

Office of Management and Budget’s Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards 2 CFR 200 – Frequently Asked Questions

.331-10 Requirements for Pass-Through Entities. Timing of Subrecipient Risk Assessments, states in part:

Section §200.331 (b) indicates that pass-through entities must “evaluate each subrecipient’s risk of noncompliance with Federal statutes, regulations, and the terms and conditions of the subaward for purposes of determining the appropriate subrecipient monitoring...” Are pass-through entities required to assess the risk of non-compliance for each applicant prior to issuing a subaward?

No. While section §200.331 (b) requires risk assessments of subrecipients, there is no requirement for pass-through entities to perform these assessments before making subawards. Under the Uniform Guidance, the purpose of these risk assessments is for pass-through entities to determine appropriate subrecipient monitoring. Pass-through entities may use judgment regarding the most appropriate timing for the assessments. Regardless of the timing chosen, the pass-through entity should document its procedures for assessing risk. Section §200.331 (b) (1)– (4) includes factors that a pass-through entity may consider when assessing subrecipient risk.

2018-013 **The Department of Transportation did not have adequate internal controls over and did not comply with requirements to collect certified payrolls from contractors on projects funded by the Highway Planning and Construction Cluster.**

Federal Awarding Agency: U.S. Department of Transportation
Pass-Through Entity: None
CFDA Number and Title: 20.205 Highway Planning and Construction Cluster
20.219
20.224
Federal Award Number: Too numerous to list. All approved sub-award projects under the Stewardship and Oversight Agreement
Applicable Compliance Component: Special Tests and Provisions: Wage Rate Requirements
Known Questioned Cost Amount: None

Background

The Washington State Department of Transportation (Department) receives federal funding under the Highway Planning and Construction Cluster for highway construction projects throughout the state. Some of these projects are awarded to contractors who perform the work on behalf of the Department. The Department spent about \$616 million in federal Highway Planning and Construction Cluster funds during fiscal year 2018.

All laborers and mechanics employed by contractors or subcontractors to work on construction contracts exceeding \$2,000 financed by federal assistance funds must be paid wages not less than those established for the locality of the project (prevailing wage rates) by the Department of Labor. All contractors and subcontractors are required to submit a copy of their payroll and a statement of compliance (certified payrolls) for each week in which any applicable contract work is performed.

There are two types of construction contracts: Design-build and design-bid-build. Under a design-build contract, the contractor will engineer the project and build it. In a design-bid-build contract, the Department engineers the project and the contractor builds it based on the Department’s plans. On both types of contracts, there is a prime contractor and subcontractors. The design-build contractor is the prime contractor on design-build projects.

The Department has field inspectors on-site during construction work to ensure projects are completed in accordance with contract specifications. For every day of the week when contract work is performed, the inspector completes an Inspector Daily Report (IDR) and documents if there was any labor or mechanical work that day. The IDRs are submitted to the project office, which reviews them to determine if any contractors are required to submit certified payrolls for that week.

The Department publishes the *Standard Specifications for Road, Bridge, and Municipal Construction*, which requires contractors to submit certified payrolls to the Department within 10 calendar days of the end of each weekly payroll period. It also specifies that if their certifications are not submitted in a timely manner, the Department can withhold payment from contractors and enact other sanctions as necessary.

Description of Condition

The Department did not have adequate internal controls over and did not comply with requirements to collect certified payrolls from contractors on projects funded by the Highway Planning and Construction Cluster.

We used a statistical sampling method and randomly sampled 59 weeks in which work was performed on a specific construction contract. The 59 weeks included 270 certified payrolls collected for prime contractors and subcontractors under 46 different contracts.

Collecting certified payroll

The Department did not collect all certified payrolls as required. Based on the IDRs completed by Department field inspectors, we determined certified payrolls were missing for five of the 59 weeks we examined. These five weeks were missing 11 of 49 required certified payrolls.

Of the 270 certified payrolls we examined, 119 were not submitted within 10 calendar days as required. On average, these payrolls were 39 days late, and seven were over 200 days late.

For an additional 132 certified payrolls, we could not determine if they were collected in a timely manner because the Department did not document when they were received.

Internal controls and review of certified payroll

For 13 of the 59 weeks examined, we found inconsistencies between what was reported on the IDRs, what was recorded in the documentation used to track certified payroll and the certified payroll forms:

- For one contract that used a design-build contractor, we reviewed two separate weeks. The Department provided 53 contractor files in response to our request for certified payroll documentation. We determined:
 - Eighteen of these contractors were on the IDRs completed by the Department, but were not on the IDRs completed by the design-build contractor. Three of these 18 contractors also were not on the Department's tracking spreadsheet.
 - Of the remaining 35 contractors, 33 were not on any of the IDRs. Two contractors were on the IDRs completed by the design-build contractor, but were not on the Department's IDRs; certified payroll was provided for these two contractors.
 - Certified payrolls were provided for 29 of the contractors that were not on any IDRs.
- For two weeks, a contractor was reported on the IDR but was not on the documentation used to track certified payroll.
- For one week, the certified payroll was dated as being submitted six days before the end of the pay period.
- For one week, the certified payroll submitted by one contractor lacked the signature page.

We consider these internal control deficiencies to be a material weakness.

This condition was not reported in the prior audit.

Cause of Condition

Management did not adequately monitor to ensure compliance with federal requirements. There were no written policies and procedures describing how staff should collect and account for all required certified payroll.

According to Department headquarters, the project offices should be using a tracking mechanism, such as a spreadsheet, to ensure all required certified payrolls are collected from the contractor. However, Department headquarters staff also said they do not provide a specific form for project offices to use or procedure to follow and leave it up to each project office to determine their tracking method. Project offices are allowed discretion in how to operate their offices. Offices vary in size and workload.

Staff in two different project offices told us they do not have any documentation or method for ensuring all required certified payrolls are collected. Staff in a third project office said they had never been provided with any instruction or standard processes for collecting and tracking certified payroll.

Effect of Condition

When the Department does not collect all certified payrolls, it cannot ensure that laborers under federally funded construction contracts are paid the applicable prevailing wages as required by law.

Recommendations

We recommend the Department:

- Establish written policies and procedures for staff to follow to ensure all required certified payrolls are collected from the contractor in a timely manner
- Collect the certified payroll from all prime contractors and subcontractors for each week in which labor and/or mechanical work was performed within 10 days of the week ending, as required

Department's Response

We appreciate the State Auditor's Office (SAO) audit of the Federal Highway Program. WSDOT is committed to ensuring our programs comply with federal regulations.

After consulting with the Federal Highway Administration (FHWA) and our additional research, we believe our process complies with the Davis-Bacon Act and federal regulations for contractor payment of prevailing wages. Please consider FHWA's February 6, 2019 email in support of our agency's compliance with the regulations at issue, as referenced in our technical response of February 8th.

The draft audit finding did not take into account the nature of the contractual relationship between the contractor and WSDOT as the owner. The owner's compliance with the Davis-Bacon Act and regulations cited in the finding is determined by collective actions and not merely by how many payrolls are collected from the contractor within a 10 day window. WSDOT, in close consultation with FHWA, has established a contract administration processes with contingencies built in to address and correct for contractor noncompliance. WSDOT and the contractor share the responsibility to apply and enforce

the prevailing wage rate requirements in Federal-aid contracts. FHWA guidance recommends actions to take if a contractor is habitually late in submitting payrolls, but leaves it up to WSDOT to determine when sanctions should be imposed. WSDOT's Standard Specifications (1-07 .9(5)) on certified payrolls aligns with FHWA guidance. Sanctions are imposed as appropriate during the life of a contract.

Further, WSDOT will not close a project until they have addressed all certified payrolls. Through additional research, the WSDOT Construction Office has confirmed that our project offices have collected all but one of the 262 certified payrolls in question, and has taken action, such as withholding of funds, against contractors who submitted payrolls habitually late.

We will continue to look for opportunities to improve our process as well as our documentation to demonstrate compliance with the Davis-Bacon Act requirements. We will consult with FHWA for any further actions needed to resolve this finding.

Auditor's Concluding Remarks

The Department states it confirmed all but one certified payroll was received, which is not consistent with our audit results. After performing our testing, we provided the results to management and gave the Department the opportunity to provide additional documentation for our review. No further documentation was provided by the Department.

The Department states it has processes in place to ensure compliance is achieved before a construction project closes. The purpose of collecting certifications timely, however, is so the Department can ensure workers on federal projects they oversee are being paid the proper wages. Collecting them significantly late does not allow for non-compliance to be detected and addressed in a timely manner.

We reaffirm our finding and will review the status of the Department's corrective action during our next audit.

Applicable Laws and Regulations

Title 2 U.S. Code of Federal Regulations Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance) establishes the following applicable requirements:

Section 200.303 Internal controls, states in part:

The non-Federal entity must:

- (a) Establish and maintain effective internal control over the Federal award that provides reasonable assurance that the non-Federal entity is managing the Federal award in compliance with Federal statutes, regulations, and the terms and conditions of the Federal award. These internal controls should be in compliance with guidance in "Standards for Internal Control in the Federal Government" issued by the Comptroller General of the United States or the "Internal Control Integrated Framework", issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).
- (b) Comply with Federal statutes, regulations, and the terms and conditions of the Federal awards.

- (d) Take prompt action when instances of noncompliance are identified including noncompliance identified in audit findings.

Section 200.516 Audit findings, states in part:

- (a) *Audit findings reported.* The auditor must report the following as audit findings in a schedule of findings and questioned costs:
 - (1) Significant deficiencies and material weaknesses in internal control over major programs and significant instances of abuse relating to major programs. The auditor's determination of whether a deficiency in internal control is a significant deficiency or material weakness for the purpose of reporting an audit finding is in relation to a type of compliance requirement for a major program identified in the Compliance Supplement.
 - (2) Material noncompliance with the provisions of Federal statutes, regulations, or the terms and conditions of Federal awards related to a major program. The auditor's determination of whether a noncompliance with the provisions of Federal statutes, regulations, or the terms and conditions of Federal awards is material for the purpose of reporting an audit finding is in relation to a type of compliance requirement for a major program identified in the compliance supplement.

The American Institute of Certified Public Accountants defines significant deficiencies and material weaknesses in internal controls over compliance in its *Codification of Statements on Auditing Standards*, section 935, Compliance Audits, as follows:

- .11 For purposes of adapting GAAS to a compliance audit, the following terms have the meanings attributed as follows: ...

Deficiency in internal control over compliance. A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance on a timely basis. A deficiency in design exists when (a) a control necessary to meet the control objective is missing, or (b) an existing control is not properly designed so that, even if the control operates as designed, the control objective would not be met. A deficiency in operation exists when a properly designed control does not operate as designed or the person performing the control does not possess the necessary authority or competence to perform the control effectively.

Material weakness in internal control over compliance. A deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a compliance requirement will not be prevented, or detected and corrected, on a timely basis. In this section, a reasonable possibility exists when the likelihood of an event occurring is either reasonably possible or probable as defined as follows:

Reasonably possible. The chance of the future event or events occurring is more than remote but less than likely.

Probable. The future event or events are likely to occur.

Significant deficiency in internal control over compliance. A deficiency, or a combination of deficiencies, in internal control over compliance that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

Material noncompliance. In the absence of a definition of material noncompliance in the governmental audit requirement, a failure to follow compliance requirements or a violation of prohibitions included in the applicable compliance requirements that results in noncompliance that is quantitatively or qualitatively material, either individually or when aggregated with other noncompliance, to the affected government program.

Title 29, Code of Federal Regulations contains, in part:

5.5 Contract provisions and related matters.

(a) The Agency head shall cause or require the contracting officer to insert in full in any contract in excess of \$2,000 which is entered into for the actual construction, alteration and/or repair, including painting and decorating, of a public building or public work, or building or work financed in whole or in part from Federal funds or in accordance with guarantees of a Federal agency or financed from funds obtained by pledge of any contract of a Federal agency to make a loan, grant or annual contribution (except where a different meaning is expressly indicated), and which is subject to the labor standards provisions of any of the acts listed in §5.1, the following clauses (or any modifications thereof to meet the particular needs of the agency, *Provided*, That such modifications are first approved by the Department of Labor):

(1) *Minimum wages.* (i) All laborers and mechanics employed or working upon the site of the work (or under the United States Housing Act of 1937 or under the Housing Act of 1949 in the construction or development of the project), will be paid unconditionally and not less often than once a week, and without subsequent deduction or rebate on any account (except such payroll deductions as are permitted by regulations issued by the Secretary of Labor under the Copeland Act (29 CFR part 3)), the full amount of wages and bona fide fringe benefits (or cash equivalents thereof) due at time of payment computed at rates not less than those contained in the wage determination of the Secretary of Labor which is attached hereto and made a part hereof, regardless of any contractual relationship which may be alleged to exist between the contractor and such laborers and mechanics. Contributions made or costs reasonably anticipated for bona fide fringe benefits under section 1(b)(2) of the Davis-Bacon Act on behalf of laborers or mechanics are considered wages paid to such laborers or mechanics, subject to the provisions of paragraph (a)(1)(iv) of this section; also, regular contributions made or costs incurred for more than a weekly period (but not less often than quarterly) under plans, funds, or programs which cover the particular weekly period, are deemed to be constructively made or incurred during such weekly period. Such laborers and mechanics shall be paid the appropriate wage rate and fringe benefits on the wage determination for the classification of work actually performed, without regard to skill, except as provided in §5.5(a)(4). Laborers or mechanics performing work in more than one classification may be compensated at the rate specified for each classification for

the time actually worked therein: *Provided*, that the employer's payroll records accurately set forth the time spent in each classification in which work is performed. The wage determination (including any additional classification and wage rates conformed under paragraph (a)(1)(ii) of this section) and the Davis-Bacon poster (WH-1321) shall be posted at all times by the contractor and its subcontractors at the site of the work in a prominent and accessible place where it can be easily seen by the workers.

- (ii) (A) The contractor shall submit weekly for each week in which any contract work is performed a copy of all payrolls to the (write in name of appropriate federal agency) if the agency is a party to the contract, but if the agency is not such a party, the contractor will submit the payrolls to the applicant, sponsor, or owner, as the case may be, for transmission to the (write in name of agency). The payrolls submitted shall set out accurately and completely all of the information required to be maintained under 29 CFR 5.5(a)(3)(i), except that full social security numbers and home addresses shall not be included on weekly transmittals. Instead the payrolls shall only need to include an individually identifying number for each employee (*e.g.*, the last four digits of the employee's social security number). The required weekly payroll information may be submitted in any form desired. Optional Form WH-347 is available for this purpose from the Wage and Hour Division Web site at <http://www.dol.gov/esa/whd/forms/wh347instr.htm> or its successor site. The prime contractor is responsible for the submission of copies of payrolls by all subcontractors. Contractors and subcontractors shall maintain the full social security number and current address of each covered worker, and shall provide them upon request to the (write in name of appropriate federal agency) if the agency is a party to the contract, but if the agency is not such a party, the contractor will submit them to the applicant, sponsor, or owner, as the case may be, for transmission to the (write in name of agency), the contractor, or the Wage and Hour Division of the Department of Labor for purposes of an investigation or audit of compliance with prevailing wage requirements. It is not a violation of this section for a prime contractor to require a subcontractor to provide addresses and social security numbers to the prime contractor for its own records, without weekly submission to the sponsoring government agency (or the applicant, sponsor, or owner).
- (B) Each payroll submitted shall be accompanied by a "Statement of Compliance," signed by the contractor or subcontractor or his or her agent who pays or supervises the payment of the persons employed under the contract and shall certify the following:
 - (1) That the payroll for the payroll period contains the information required to be provided under §5.5 (a)(3)(ii) of Regulations, 29 CFR part 5, the appropriate information is being maintained under §5.5 (a)(3)(i) of Regulations, 29 CFR part 5, and that such information is correct and complete;
 - (2) That each laborer or mechanic (including each helper, apprentice, and trainee) employed on the contract during the payroll period has been paid the full weekly wages earned, without rebate, either directly or indirectly, and that no deductions have been made either directly or indirectly from the full wages earned, other than permissible deductions as set forth in Regulations, 29 CFR part 3;

- (3) That each laborer or mechanic has been paid not less than the applicable wage rates and fringe benefits or cash equivalents for the classification of work performed, as specified in the applicable wage determination incorporated into the contract.
- (C) The weekly submission of a properly executed certification set forth on the reverse side of Optional Form WH-347 shall satisfy the requirement for submission of the “Statement of Compliance” required by paragraph (a)(3)(ii)(B) of this section.
- (6) *Subcontracts.* The contractor or subcontractor shall insert in any subcontracts the clauses contained in 29 CFR 5.5(a)(1) through (10) and such other clauses as the (write in the name of the Federal agency) may by appropriate instructions require, and also a clause requiring the subcontractors to include these clauses in any lower tier subcontracts. The prime contractor shall be responsible for the compliance by any subcontractor or lower tier subcontractor with all the contract clauses in 29 CFR 5.5.
- (7) *Contract termination: debarment.* A breach of the contract clauses in 29 CFR 5.5 may be grounds for termination of the contract, and for debarment as a contractor and a subcontractor as provided in 29 CFR 5.12.
- (8) *Compliance with Davis-Bacon and Related Act requirements.* All rulings and interpretations of the Davis-Bacon and Related Acts contained in 29 CFR parts 1, 3, and 5 are herein incorporated by reference in this contract.

Standard Specifications for Road, Bridge, and Municipal Construction 2018 states, in part:

1-07.9(5) Required Documents

Certified payrolls are required to be submitted by the Contractor to the Engineer, for the Contractor and all Subcontractors or lower tier subcontractors, on all Federal-aid projects and, when requested in writing by the Engineer, on projects funded with only Contracting Agency funds. If these payrolls are not supplied within 10 calendar days of the end of the preceding weekly payroll period for Federal-aid projects or within 10 calendar days from the date of the written request on projects with only Contracting Agency funds, any or all payments may be withheld until compliance is achieved. Also, failure to provide these payrolls could result in other sanctions as provided by State laws (RCW 39.12.050) and/or Federal regulations (29 CFR 5.12). All certified payrolls shall be complete and explicit. Employee labor descriptions used on certified payrolls shall coincide exactly with the labor descriptions listed on the minimum wage schedule in the Contract unless the Engineer approves an alternate method to identify the labor used by the Contractor to compare with the labor listed in the Contract Provisions. When an apprentice is shown on the certified payroll at a rate less than the minimum prevailing journey wage rate, the apprenticeship registration number for that employee from the State Apprenticeship and Training Council shall be shown along with the correct employee classification code.

2018-014 The Department of Transportation did not have adequate internal controls over and did not comply with requirements to collect certified payrolls from contractors on projects funded by the Federal Transit Cluster.

Federal Awarding Agency: U.S. Department of Transportation
Pass-Through Entity: None
CFDA Number and Title: 20.500 Federal Transit – Capital Investment Grants (Fixed Guideway Capital Investment Grants)
20.507 Federal Transit – Formula Grants (Urbanized Area Formula Program)
20.525 State of Good Repair Grants Program
20.526 Bus and Bus Facilities Formula Program
Federal Award Number: WA-2016-028-00; WA-2016-029-00; WA-2017-022-00; WA-2017-024-00; WA-2018-006-01; WA-2018-021-01; WA-90-X604-00
Applicable Compliance Component: Special Tests and Provisions: Wage Rate Requirements
Known Questioned Cost Amount: None

Background

The Washington State Department of Transportation (Department), State Ferries Division, receives federal funding under the Federal Transit Cluster to fund projects for:

- Constructing new or extending fixed guideway systems or corridor based rapid transit systems
- Assisting in financing the planning, acquisition, construction, preventive maintenance and improvement of facilities and equipment in public transportation services
- Maintaining, rehabilitating and replacing transit assets for fixed guideway transit systems

Some of these projects are awarded to contractors who perform the work on behalf of the Department. The Department administers and oversees federally funded construction projects, including construction and renovation of ferry terminals, as well as the construction of new, or preservation of existing, ferry vessels. The Department spent almost \$70 million in Federal Transit Cluster funds during fiscal year 2018.

All laborers and mechanics employed by contractors or subcontractors to work on construction contracts exceeding \$2,000 financed by federal assistance funds must be paid wages not less than those established for the locality of the project (prevailing wage rates) by the Department of Labor. All contractors and subcontractors are required to submit a copy of their payroll and a statement of compliance (certified payrolls) for each week in which any applicable contract work is performed.

The Department has field inspectors onsite during construction work to ensure projects are completed in accordance with contract specifications and federal guidelines. For every day of the week when contract work is performed, the inspector completes an Inspector Daily Report (IDR) and documents if there was any labor or mechanical work performed that day. The IDRs are submitted to the project

office, which reviews them to determine if any contractors are required to submit certified payrolls for that week.

The Department publishes the *Standard Specifications for Road, Bridge, and Municipal Construction*, which requires contractors to submit certified payrolls to the Department within 10 calendar days of the end of each weekly payroll period. It also specifies that if their certifications are not submitted in a timely manner, the Department can withhold payment from contractors and enact other sanctions as necessary.

Description of Condition

The Department did not have adequate internal controls over and did not comply with requirements to collect certified payrolls from contractors on projects funded by the Federal Transit Cluster.

We used a non-statistical sampling method to select 15 out of 105 weeks in which work was performed on a specific construction contract. The 15 weeks included 111 certified payrolls collected for prime contractors and subcontractors under four different federally funded contracts.

Collecting certified payrolls

The Department did not collect all certified payrolls as required. Based on the IDRs completed by Department field inspectors, we determined certified payrolls were missing for three of the 15 weeks we examined. These three weeks were missing three of 11 required certified payrolls.

Of the 111 certified payrolls we examined, 46 were not submitted within 10 calendar days as required. On average, these payrolls were 20 days late. Five were over 60 days late.

For an additional three certified payrolls, we could not determine if they were collected in a timely manner because the Department did not document when they were received. We also identified two certified payrolls that did not contain a Statement of Compliance signed by the preparer (either the prime contractor, or a subcontractor).

Internal controls and review of certified payroll

For eight of the 15 weeks examined, we found inconsistencies between what was reported on the IDRs, what was recorded in the documentation used to track certified payroll, and the supporting documentation received from the contractors:

- For six weeks, certified payrolls were provided for 10 contractors that were not on any IDRs.
- For three weeks, the IDRs indicated four contractors performed labor; however three of the four contractors submitted Statements of No Work Performed. The fourth contractor did not submit a certified payroll until two months after the audit period ended, which was received about 10 months after the corresponding payroll period ended.
- For three weeks, contractors were listed in the IDR but were not on the documentation used to track certified payroll.
- For two weeks, the certified payroll submitted by one contractor lacked a signature.

We consider these internal control deficiencies to be a material weakness.

This condition was not reported in the prior audit.

Cause of Condition

Management did not adequately monitor to ensure compliance with federal requirements. There were no written policies and procedures describing how staff should collect and account for all required certified payroll.

According to Department headquarters, the project offices should be using a tracking mechanism, such as a spreadsheet, to ensure all required certified payrolls are collected from the contractor. However, there is no standardized form for project offices to use or procedure to follow to track certified weekly payrolls. Project offices are permitted to determine their own tracking method for contracts under their supervision.

In addition, Chief Inspectors and Project Engineers did not adequately review IDRs to identify all contractors required to submit certified payrolls for the corresponding week. In the case of certified payrolls that were never provided by the contractor, the discrepancies between payroll that was submitted and the vendors listed by the Site Inspectors in the IDR were not detected and communicated to those responsible for processing the vendor pay estimates.

Effect of Condition

When the Department does not collect all certified payrolls, it cannot ensure that laborers under federally funded construction contracts are paid the local prevailing wages as required by law. By not collecting certified payrolls weekly, the Department is not complying with federal requirements, and may be subject to actions by the federal grantor.

Recommendations

We recommend the Department:

- Establish written policies and procedures for staff to follow to ensure all required certified payrolls are collected from the contractor in a timely manner
- Collect the certified payrolls from all prime contractors and subcontractors for each week in which labor and/or mechanical work was performed within 10 days of the week ending, as required
- Consider assessing sanctions on noncompliant contractors in accordance with the Standard Specifications, such as withholding any or all payments, as necessary when certified payroll is not submitted within 10 days as required

Department's Response

We appreciate the State Auditor's Office (SAO) audit of the Federal Transit Administration Program. WSDOT is committed to ensuring our programs comply with federal regulations.

After consulting with both the Federal Transit Administration (FTA) and the Federal Highway Administration (FHWA) and our additional research, we believe our process complies with the Davis-Bacon Act and federal regulations for contractor payment of prevailing wages.

The draft audit finding did not take into account the nature of the contractual relationship between the contractor and WSDOT as the owner. The owner's compliance with the Davis-Bacon Act and regulations cited in the finding is determined by collective actions and not merely by how many payrolls are collected from the contractor within a 10 day window. WSDOT has established a contract administration processes with contingencies built in to address and correct for contractor noncompliance. WSDOT and the contractor share the responsibility to apply and enforce the prevailing wage rate requirements in Federal-aid contracts. Federal guidance recommends actions to take if a contractor is habitually late in submitting payrolls, but leaves it up to WSDOT to determine when sanctions should be imposed. WSDOT's Standard Specifications (1-07.9(5)) on certified payrolls aligns with this federal guidance. Sanctions are imposed as appropriate during the life of a contract.

Further, WSDOT will not close a project until they have addressed all certified payrolls. Through additional research, the WSDOT Ferries Division has confirmed that we have collected all of the 52 certified payrolls in question, and have taken action or will take action in case of open contracts, such as withholding of funds, against contractors who submitted payrolls habitually late.

We will continue to look for opportunities to improve our process as well as our documentation to demonstrate compliance with the Davis-Bacon Act requirements. We will consult with FTA for any further actions needed to resolve this finding.

Auditor's Concluding Remarks

The Department states it confirmed all certified payrolls were received, which is not consistent with our audit results. After performing our testing, we provided the results to management and gave the Department the opportunity to provide additional documentation for our review. No further documentation was provided by the Department.

The Department states it has processes in place to ensure compliance is achieved before a construction project closes. The purpose of collecting certifications timely, however, is so the Department can ensure workers on federal projects they oversee are being paid the proper wages. Collecting them significantly late does not allow for non-compliance to be detected and addressed in a timely manner.

We reaffirm our finding and will review the status of the Department's corrective action during our next audit.

Applicable Laws and Regulations

Title 2 U.S. Code of Federal Regulations Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance) establishes the following applicable requirements:

Section 200.303 Internal controls, states in part:

The non-Federal entity must:

- (a) Establish and maintain effective internal control over the Federal award that provides reasonable assurance that the non-Federal entity is managing the Federal award in compliance with Federal statutes, regulations, and the terms and conditions of the Federal award. These internal controls should be in compliance with guidance in “Standards for Internal Control in the Federal Government” issued by the Comptroller General of the United States or the “Internal Control Integrated Framework”, issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).
- (b) Comply with Federal statutes, regulations, and the terms and conditions of the Federal awards.
- (d) Take prompt action when instances of noncompliance are identified including noncompliance identified in audit findings.

Section 200.516 Audit findings, states in part:

- (a) *Audit findings reported.* The auditor must report the following as audit findings in a schedule of findings and questioned costs:
 - (1) Significant deficiencies and material weaknesses in internal control over major programs and significant instances of abuse relating to major programs. The auditor’s determination of whether a deficiency in internal control is a significant deficiency or material weakness for the purpose of reporting an audit finding is in relation to a type of compliance requirement for a major program identified in the Compliance Supplement.
 - (2) Material noncompliance with the provisions of Federal statutes, regulations, or the terms and conditions of Federal awards related to a major program. The auditor’s determination of whether a noncompliance with the provisions of Federal statutes, regulations, or the terms and conditions of Federal awards is material for the purpose of reporting an audit finding is in relation to a type of compliance requirement for a major program identified in the compliance supplement.

The American Institute of Certified Public Accountants defines significant deficiencies and material weaknesses in internal controls over compliance in its *Codification of Statements on Auditing Standards*, section 935, Compliance Audits, as follows:

.11 For purposes of adapting GAAS to a compliance audit, the following terms have the meanings attributed as follows: ...

Deficiency in internal control over compliance. A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to

prevent, or detect and correct, noncompliance on a timely basis. A deficiency in design exists when (a) a control necessary to meet the control objective is missing, or (b) an existing control is not properly designed so that, even if the control operates as designed, the control objective would not be met. A deficiency in operation exists when a properly designed control does not operate as designed or the person performing the control does not possess the necessary authority or competence to perform the control effectively.

Material weakness in internal control over compliance. A deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a compliance requirement will not be prevented, or detected and corrected, on a timely basis. In this section, a reasonable possibility exists when the likelihood of an event occurring is either reasonably possible or probable as defined as follows:

Reasonably possible. The chance of the future event or events occurring is more than remote but less than likely.

Probable. The future event or events are likely to occur.

Significant deficiency in internal control over compliance. A deficiency, or a combination of deficiencies, in internal control over compliance that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

Material noncompliance. In the absence of a definition of material noncompliance in the governmental audit requirement, a failure to follow compliance requirements or a violation of prohibitions included in the applicable compliance requirements that results in noncompliance that is quantitatively or qualitatively material, either individually or when aggregated with other noncompliance, to the affected government program.

Title 29, Code of Federal Regulations contains, in part:

5.5 Contract provisions and related matters.

(a) The Agency head shall cause or require the contracting officer to insert in full in any contract in excess of \$2,000 which is entered into for the actual construction, alteration and/or repair, including painting and decorating, of a public building or public work, or building or work financed in whole or in part from Federal funds or in accordance with guarantees of a Federal agency or financed from funds obtained by pledge of any contract of a Federal agency to make a loan, grant or annual contribution (except where a different meaning is expressly indicated), and which is subject to the labor standards provisions of any of the acts listed in §5.1, the following clauses (or any modifications thereof to meet the particular needs of the agency, *Provided*, That such modifications are first approved by the Department of Labor):

(1) *Minimum wages.* (i) All laborers and mechanics employed or working upon the site of the work (or under the United States Housing Act of 1937 or under the Housing Act of 1949 in the construction or development of the project), will be paid unconditionally and not less often than once a week, and without subsequent deduction or rebate on any account (except such payroll deductions as are permitted by regulations issued by the Secretary of Labor under the Copeland Act (29 CFR part 3)), the full amount of wages and bona fide fringe benefits (or cash equivalents

thereof) due at time of payment computed at rates not less than those contained in the wage determination of the Secretary of Labor which is attached hereto and made a part hereof, regardless of any contractual relationship which may be alleged to exist between the contractor and such laborers and mechanics. Contributions made or costs reasonably anticipated for bona fide fringe benefits under section 1(b)(2) of the Davis-Bacon Act on behalf of laborers or mechanics are considered wages paid to such laborers or mechanics, subject to the provisions of paragraph (a)(1)(iv) of this section; also, regular contributions made or costs incurred for more than a weekly period (but not less often than quarterly) under plans, funds, or programs which cover the particular weekly period, are deemed to be constructively made or incurred during such weekly period. Such laborers and mechanics shall be paid the appropriate wage rate and fringe benefits on the wage determination for the classification of work actually performed, without regard to skill, except as provided in §5.5(a)(4). Laborers or mechanics performing work in more than one classification may be compensated at the rate specified for each classification for the time actually worked therein: *Provided*, that the employer's payroll records accurately set forth the time spent in each classification in which work is performed. The wage determination (including any additional classification and wage rates conformed under paragraph (a)(1)(ii) of this section) and the Davis-Bacon poster (WH-1321) shall be posted at all times by the contractor and its subcontractors at the site of the work in a prominent and accessible place where it can be easily seen by the workers.

- (ii) (A) The contractor shall submit weekly for each week in which any contract work is performed a copy of all payrolls to the (write in name of appropriate federal agency) if the agency is a party to the contract, but if the agency is not such a party, the contractor will submit the payrolls to the applicant, sponsor, or owner, as the case may be, for transmission to the (write in name of agency). The payrolls submitted shall set out accurately and completely all of the information required to be maintained under 29 CFR 5.5(a)(3)(i), except that full social security numbers and home addresses shall not be included on weekly transmittals. Instead the payrolls shall only need to include an individually identifying number for each employee (*e.g.*, the last four digits of the employee's social security number). The required weekly payroll information may be submitted in any form desired. Optional Form WH-347 is available for this purpose from the Wage and Hour Division Web site at <http://www.dol.gov/esa/whd/forms/wh347instr.htm> or its successor site. The prime contractor is responsible for the submission of copies of payrolls by all subcontractors. Contractors and subcontractors shall maintain the full social security number and current address of each covered worker, and shall provide them upon request to the (write in name of appropriate federal agency) if the agency is a party to the contract, but if the agency is not such a party, the contractor will submit them to the applicant, sponsor, or owner, as the case may be, for transmission to the (write in name of agency), the contractor, or the Wage and Hour Division of the Department of Labor for purposes of an investigation or audit of compliance with prevailing wage requirements. It is not a violation of this section for a prime contractor to require a subcontractor to provide addresses and social security

numbers to the prime contractor for its own records, without weekly submission to the sponsoring government agency (or the applicant, sponsor, or owner).

- (B) Each payroll submitted shall be accompanied by a "Statement of Compliance," signed by the contractor or subcontractor or his or her agent who pays or supervises the payment of the persons employed under the contract and shall certify the following:
- (1) That the payroll for the payroll period contains the information required to be provided under §5.5 (a)(3)(ii) of Regulations, 29 CFR part 5, the appropriate information is being maintained under §5.5 (a)(3)(i) of Regulations, 29 CFR part 5, and that such information is correct and complete;
 - (2) That each laborer or mechanic (including each helper, apprentice, and trainee) employed on the contract during the payroll period has been paid the full weekly wages earned, without rebate, either directly or indirectly, and that no deductions have been made either directly or indirectly from the full wages earned, other than permissible deductions as set forth in Regulations, 29 CFR part 3;
 - (3) That each laborer or mechanic has been paid not less than the applicable wage rates and fringe benefits or cash equivalents for the classification of work performed, as specified in the applicable wage determination incorporated into the contract.
- (C) The weekly submission of a properly executed certification set forth on the reverse side of Optional Form WH-347 shall satisfy the requirement for submission of the "Statement of Compliance" required by paragraph (a)(3)(ii)(B) of this section.
- (6) *Subcontracts.* The contractor or subcontractor shall insert in any subcontracts the clauses contained in 29 CFR 5.5(a)(1) through (10) and such other clauses as the (write in the name of the Federal agency) may by appropriate instructions require, and also a clause requiring the subcontractors to include these clauses in any lower tier subcontracts. The prime contractor shall be responsible for the compliance by any subcontractor or lower tier subcontractor with all the contract clauses in 29 CFR 5.5.
- (7) *Contract termination: debarment.* A breach of the contract clauses in 29 CFR 5.5 may be grounds for termination of the contract, and for debarment as a contractor and a subcontractor as provided in 29 CFR 5.12.
- (8) *Compliance with Davis-Bacon and Related Act requirements.* All rulings and interpretations of the Davis-Bacon and Related Acts contained in 29 CFR parts 1, 3, and 5 are herein incorporated by reference in this contract.

Standard Specifications for Road, Bridge, and Municipal Construction 2018 states, in part:

1-07.9(5) Required Documents

Certified payrolls are required to be submitted by the Contractor to the Engineer, for the Contractor and all Subcontractors or lower tier subcontractors, on all Federal-aid projects and, when requested in writing by the Engineer, on projects funded with only Contracting Agency funds. If these payrolls are not supplied within 10 calendar days of the end of the [preceding](#) weekly payroll period for Federal-aid projects or within 10 calendar days from the date of the written request on projects with only Contracting Agency funds, any or all payments may be withheld until compliance is achieved. Also,

failure to provide these payrolls could result in other sanctions as provided by State laws (RCW 39.12.050) and/or Federal regulations (29 CFR 5.12). All certified payrolls shall be complete and explicit. Employee labor descriptions used on certified payrolls shall coincide exactly with the labor descriptions listed on the minimum wage schedule in the Contract unless the Engineer approves an alternate method to identify the labor used by the Contractor to compare with the labor listed in the Contract Provisions. When an apprentice is shown on the certified payroll at a rate less than the minimum prevailing journey wage rate, the apprenticeship registration number for that employee from the State Apprenticeship and Training Council shall be shown along with the correct employee classification code.

2018-015

The Department of Transportation, State Ferries Division, did not have adequate internal controls over and did not comply with equipment management requirements.

Federal Awarding Agency: U.S. Department of Transportation
Pass-Through Entity: None
CFDA Number and Title: 20.500 Federal Transit – Capital Investment Grants (Fixed Guideway Capital Investment Grants; Section 5309)
20.507 Federal Transit – Formula Grants (Urbanized Area Formula Program; Section 5307)
20.525 State of Good Repair Grants Program (Section 5337)
20.526 Bus and Bus Facilities Formula Program
Federal Award Number: WA-2016-028-00; WA-2016-029-00; WA-2017-022-00; WA-2017-024-00; WA-2018-006-01; WA-2018-021-01; WA-90-X604-00
Applicable Compliance Component: Equipment and Real Property Management
Known Questioned Cost Amount: None

Background

The Washington State Department of Transportation (Department), State Ferries Division (Division), receives federal funding under the Federal Transit Cluster to fund projects for:

- Constructing new or extending fixed guideway systems, or corridor based rapid transit systems
- Assisting in financing the planning, acquisition, construction, preventive maintenance, and improvement of facilities and equipment in public transportation services
- Maintaining, rehabilitating and replacing transit assets for fixed guideway transit systems

The Department receives federal grant funds to purchase equipment for ferry vessels as well as for maintenance, preservation, and improvement activities. The Division operates the largest ferry system in the United States, transporting over 25 million passengers annually to 20 different ports within Washington and British Columbia. There are currently 23 ferry vessels in operation.

To sustain its ferry operations, the Division purchases ferry parts and equipment from approved distributors of electromotive-diesel engine components. These components are purchased to replace engines approaching the end of their useful life, or vital engine components in need of repair. Equipment acquired with grant funds includes full engine assemblies, radar equipment, display units, and engine rebuild kits containing turbochargers, power packs, injectors, intercoolers, water pumps and other miscellaneous components.

Federal requirements stipulate that states receiving federal funds must use, manage and dispose of equipment in accordance with the state’s laws and procedures. In Washington, the State Administrative and Accounting Manual (SAAM), published by the Office of Financial Management, specifies how

agencies must manage and account for equipment. SAAM defines equipment as tangible property other than land, buildings, improvements other than buildings, or infrastructure, which is used in state operations and with a useful life of more than one year. For these assets, agencies are required to:

- Mark and identify both capitalized and non-capitalized assets
- Conduct physical inventories of state-owned assets
- Establish a capitalized asset inventory system, which includes how to add and remove assets from the inventory
- Implement an inventory records policy
- Reconcile physical inventories
- Establish policies and procedures for reporting surplus, lost and/or stolen items

The Department's Purchasing and Materials Management Office (PMMO) is responsible for monitoring equipment and inventories for the entire Department. SAAM requires agencies to use the State's Capital Asset Management System (CAMS) to manage capitalized asset inventories. Prior written approval from the Department of Enterprise Services (DES), Office of the Chief Information Officer must be obtained by the agency if it chooses to acquire and implement an alternative inventory management system.

In fiscal year 2018, the Department acquired more than \$4.4 million of equipment with Federal funds awarded under the Federal Transit Cluster.

Description of Condition

The Department of Transportation, State Ferries Division, did not have adequate internal controls over and did not comply with equipment management requirements.

Internal controls

We identified the following internal control weaknesses:

- The Division has not established its own policies or procedures for Equipment management and inventories of equipment and did not follow other documented Department-level policies.
- The Division did not use CAMS to manage assets and did not have documented prior approval from DES to use an alternative inventory management system.
- The Department could not produce an aggregate list of all federally funded equipment acquired under the Cluster.
- The alternative inventory management system does not allow for documentation of the following required information about the equipment: the source of funding for the asset, the percentage of federal participation in the project costs for the federal award in which the asset(s) was acquired, salvage value, serial number of the asset, depreciation, useful life (in months or years) and the date of disposal.
- Division staff conducting the biennial physical inventory of equipment did not communicate results of the inventory to PMMO.
- The Department's Inventory Officer did not perform a reconciliation of the physical inventory of the Division's equipment to ensure accuracy and completeness as required. Additionally, the

Inventory Officer did not have access to the alternative inventory management system that was used by the Division.

- The most recent inventory was not done within two years of the last one as required. The Department could not provide the documentation for the prior inventory, so we could not determine how long overdue it was.

We consider these internal control deficiencies to be a material weakness.

Sampling methodology

The Division could not provide a complete report of all equipment acquired with funding awarded through the Federal Transit Cluster without reviewing purchase documentation for all historical equipment purchases. To perform testing, we obtained copies of all 16 purchase orders executed by the Division to acquire equipment, including engines and engine components, during the audit period.

We reviewed all items purchased by the Division and identified 155 items that met the state's capitalized asset threshold, which includes a per-unit cost of \$5,000 or more, and a useful life of at least one year. Because the Department did not separately track items of the same asset classification, we summarized the total purchases of each item classification from each purchase order, and arrived at a total of 48 purchases totaling about \$2.4 million in federally funded equipment.

We used a non-statistical sampling method and randomly sampled 10 of a total population of 47 equipment purchases to test for compliance with state requirements for inventory records. We also separately examined one individually significant item.

Evaluation of compliance

The property records for each of the 11 tested items (100 percent) lacked the following required fields: agency name, account code, class code, depreciation amount, ownership status (federal participation percentage), salvage value, serial number and useful life. Six of the 11 tested items were also not inventoried by the Department as part of the most recent physical inventory count.

In addition to the areas noted above, the Department did not assign an inventory control number, or asset tag to the individually significant item, which is a requirement under State policies.

This condition was not reported in the prior audit.

Cause of Condition

Internal controls

PMMO believed the Division was adhering to the requirements outlined in WSDOT inventory manuals. However, the Division was using a separate internally developed system to manage its inventory.

PMMO was not granted access to the inventory system because the Division did not inform them it was using an alternative inventory management system. The Department relied on the Division to

ensure physical inventories of all its equipment were conducted each biennial cycle without independently verifying the inventory reconciliations were accurate and complete.

The Department was not aware of the requirement to obtain approval from DES to develop and implement alternative inventory management systems for capitalized assets.

Evaluation of compliance

The Department and the Division were not aware of the fields required to be documented in agency property records for capitalized assets. The engine that did not receive an inventory control number or asset tag lacked those identifiers due to the purchase order agreement with the vendor containing a provision to ship the engine directly to the vessel shipyard, thereby bypassing the Division warehouse where items are typically sent and input into the inventory management system.

The Department did not perform the last inventory within two years of the prior one because the Inventory Agent for the Division was not instructed to inventory federally funded equipment. The Division could not produce physical inventory reports from previous years; therefore, we could not determine if federal equipment had ever been inventoried by the Division.

Effect of Condition

By not establishing adequate internal controls over its management of equipment, the Department is at a higher risk of failing to detect asset losses. Additionally, when the Department does not record the ownership status of an asset, it cannot determine whether proceeds from the sale of the item should be repaid to the federal grantor.

Recommendations

We recommend the Department:

- Improve its internal controls to ensure all additions to and removals from the Division's inventory are overseen by the appointed agency inventory officer, as required by the SAAM
- Ensure physical inventory reconciliations are verified by the Agency Inventory Officer, or their delegate, for accuracy and completeness
- Ensure Department inventory policies and procedures are followed
- Ensure a physical inventory is conducted at least every two years as required and is reconciled, and supporting documentation is maintained
- Request approval from DES to continue to use an alternative capitalized asset inventory management system or use an approved system
- Ensure its inventory management system contains all fields required under state policy
- Update existing property records for all federal equipment to include all fields required under state policy

Department's Response

We appreciate the State Auditor's Office (SAO) audit of the Federal Transit Administration Program. WSDOT is committed to ensuring our programs comply with federal regulations.

It is our position that the parts in question from the audit are not capital assets and the requirements cited in the audit finding do not apply to these parts. The parts in question have no utility to the state until they are installed on a larger assembly or depreciable asset, in this case one of our ferry vessels. Once installed, the parts cease to be a discrete item and are part of the vessel. Where an installed part meets the definition of a betterment as defined in State Administrative and Accounting Manual 30.20.20.c, then it is capitalized and depreciated as part of the vessel. Where a part does not meet the definition of a betterment, it is expensed when purchased.

We appreciate the importance of safeguarding these parts through their installation on one of our vessels and accounting for them properly. In the ordinary course of business purchased parts are delivered to the warehouse and almost immediately transferred to the vessel. Occasionally, a vessel's scheduled maintenance will be delayed due to operational needs, and parts will be stored in the warehouse.

We will follow up with the Office of Financial Management for any recommendations on accounting for the parts in question. We look forward to working with your staff in the next audit to resolve any remaining items in this finding.

Auditor's Concluding Remarks

The audit did not address how the Department depreciates or expenses its assets. We are reporting on deficiencies in how the Department tracks, safeguards and conducts inventories of its assets in order to ensure they are all accounted for. We appreciate that the Department plans to work with the Office of Financial Management as they are responsible for establishing state agency requirements for managing equipment.

We reaffirm our finding and will review the status of the Department's corrective action during our next audit.

Applicable Laws and Regulations

Title 2 U.S. Code of Federal Regulations Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance) establishes the following applicable requirements:

Section 200.303 Internal controls, states in part:

The non-Federal entity must:

- (a) Establish and maintain effective internal control over the Federal award that provides reasonable assurance that the non-Federal entity is managing the Federal award in

compliance with Federal statutes, regulations, and the terms and conditions of the Federal award. These internal controls should be in compliance with guidance in “Standards for Internal Control in the Federal Government” issued by the Comptroller General of the United States or the “Internal Control Integrated Framework”, issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).

- (b) Comply with Federal statutes, regulations, and the terms and conditions of the Federal awards.
- (d) Take prompt action when instances of noncompliance are identified including noncompliance identified in audit findings.

Section 200.313 Equipment, states in part:

- (b) A state must use, manage and dispose of equipment acquired under a Federal award by the state in accordance with state laws and procedures.

Section 200.516 Audit findings, states in part:

- (a) *Audit findings reported.* The auditor must report the following as audit findings in a schedule of findings and questioned costs:
 - (1) Significant deficiencies and material weaknesses in internal control over major programs and significant instances of abuse relating to major programs. The auditor’s determination of whether a deficiency in internal control is a significant deficiency or material weakness for the purpose of reporting an audit finding is in relation to a type of compliance requirement for a major program identified in the Compliance Supplement.
 - (2) Material noncompliance with the provisions of Federal statutes, regulations, or the terms and conditions of Federal awards related to a major program. The auditor’s determination of whether a noncompliance with the provisions of Federal statutes, regulations, or the terms and conditions of Federal awards is material for the purpose of reporting an audit finding is in relation to a type of compliance requirement for a major program identified in the compliance supplement.

The American Institute of Certified Public Accountants defines significant deficiencies and material weaknesses in internal controls over compliance in its *Codification of Statements on Auditing Standards*, section 935, Compliance Audits, as follows:

.11 For purposes of adapting GAAS to a compliance audit, the following terms have the meanings attributed as follows: ...

Deficiency in internal control over compliance. A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance on a timely basis. A deficiency in design exists when (a) a control necessary to meet the control objective is missing, or (b) an existing control is not properly designed so that, even if the control operates as designed, the control objective would not be met. A deficiency in operation exists when a properly designed control does not operate as designed or the person performing the control does not possess the necessary authority or competence to perform the control effectively.

Material weakness in internal control over compliance. A deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a compliance requirement will not be prevented, or detected and corrected, on a timely basis. In this section, a reasonable possibility exists when the likelihood of an event occurring is either reasonably possible or probable as defined as follows:

Reasonably possible. The chance of the future event or events occurring is more than remote but less than likely.

Probable. The future event or events are likely to occur.

Significant deficiency in internal control over compliance. A deficiency, or a combination of deficiencies, in internal control over compliance that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

Material noncompliance. In the absence of a definition of material noncompliance in the governmental audit requirement, a failure to follow compliance requirements or a violation of prohibitions included in the applicable compliance requirements that results in noncompliance that is quantitatively or qualitatively material, either individually or when aggregated with other noncompliance, to the affected government program.

The Washington State Office of Financial Management, State Administrative and Accounting Manual (SAAM), Chapter 30 – Capital Assets, states in part:

30.10.10 Purpose of these policies

The purpose of these policies is to establish the minimum requirements for a capital assets inventory system.

30.10.30 Applicability of these policies

This chapter is applicable to all agencies of the state of Washington as defined in RCW 43.88.040(4), unless otherwise exempted by statute or rule.

30.10.40 Responsibilities of the State Agency

Establish a capital asset inventory system (refer to subsection 30.40.30) that:

- Provides control and accountability over capital assets, and
- Gathers and maintains information needed for the preparation of financial statements.

The agency head must designate, in writing, one or more Agency Inventory Officers to be responsible for maintaining and safeguarding the agency's capital assets. Agencies are responsible for developing internal policies and procedures to protect and control the use of all capital assets.

30.20.20 When to capitalize assets

The state's capitalization policy is as follows:

- The state highway system operated by the Department of Transportation;
- Infrastructure, other than the state highway system, with a cost of \$100,000 or greater;
- Buildings, building improvements, improvements other than buildings, and leasehold improvements with a cost of \$100,000 or greater;
- All other capital assets with a unit cost (including ancillary costs) of \$5,000 or greater, or collections with a total cost of \$5,000 or greater, unless otherwise noted

30.30.10 Mark all inventoriable capital assets

Mark all inventoriable capital assets upon receipt and acceptance to identify that the property belongs to the State of Washington, except as noted in Subsection 30.30.30 below.

This identification should:

- Facilitate accounting for the asset;
- Aid in its identification if the asset is lost or stolen;
- Discourage theft; and ultimately,
- Reduce the magnitude of the state's property losses.

30.30.20 How capital assets should be marked

a. Permanently affix the identification information to the asset by using a standardized adhesive tag or inscribing the asset according to the following format:

- Washington State (or state seal insignia)
- Agency Name (or authorized abbreviation or agency number)
- Optional Bar Code, and
- Assigned Control Number

b. Agencies may determine where to place the "Washington State" identification and control number on the capital asset. However, the identification and control number should be located on the principal body of the asset, rather than a removable part.

30.30.30 When it is OK not to mark a capital asset

Occasionally, an agency will find it is impractical or impossible to mark some of its inventoriable capital assets according to these standards. For example, where a capital asset:

- Would lose significant historical or resale value (such as art collections or museum and historical collections);
- Would have its warranty negatively impacted by being permanently marked
- Is stationary in nature and is not susceptible to theft (such as land, infrastructure, buildings, improvements other than buildings, and leasehold improvements);
- Has a unique permanent serial number that can be used for identification, security and inventory control (such as vehicles); or
- Is an intangible asset that lacks physical substance.

In these cases, the identification “Washington State” or state seal insignia is not required, and the agency is to apply alternative procedures to inventory and identify such assets as “Washington State.”

30.30.50 Capital asset inventory tags and control numbers need to be controlled

Responsibility for controlling capital asset control numbers rests with the agency’s inventory officer. Agencies are to ensure that adequate controls for safeguarding unissued, mutilated, and voided capital asset inventory tags are established.

30.40.10 Which assets need to be inventoried and cataloged?

The following assets are inventoriable assets and must be carried on the property records of an agency:

All assets meeting the state’s capitalization policy (refer to Subsection 30.20.20),

30.40.30 Capital asset inventory system requirements

Agencies are to maintain a capital asset inventory system that includes records for all inventoriable assets.

Agencies are to use the Capital Asset Management System (CAMS) for all assets that meet the state’s capitalization policy. Agencies may use an alternate in-house system provided written approval from the Office of the Chief Information Officer (OCIO) is obtained prior to initiating acquisition or development of the system. Refer to Subsection 80.30.88.

The following are required to be included in the inventory records:

Agency Name and Code Number - The agency name and three-digit agency code number.

Account - For proprietary and trust fund type accounts, this is the account in which the asset is being used. This may or may not be the original purchasing account.

For governmental fund type accounts, this is the account that originally purchased the asset. For those assets acquired prior to July 1, 1982, for which an account cannot be identified or is no longer in existence, such assets are to be identified as assets of the General Fund.

Acquisition Date - The date the agency takes title to, or assumes responsibility for, an asset.

Class Code - The code assigned to a capital asset that correlates to a descriptive title. Refer to Subsection 30.50.10 for Schedule A-Capital Asset Class Codes and Useful Life Schedule.

Cost - The total cost (value) assigned to the asset. Refer to Subsection 30.20.10 for clarification.

Depreciation - The portion of the cost of a capital asset representing the expiration in the service life of the asset attributable to wear and tear, deterioration, action of the physical elements, inadequacy, and/or obsolescence which is charged systematically over the useful life of the capital asset. Refer to Subsection 30.20.70. This element is not applicable to small and attractive assets.

Description - Name of the asset.

Disposal Authorization - When required, either the number assigned by the Office of the Chief Information Officer/Technology Services Board (for information technology related equipment and proprietary software) or the Department of Enterprise Services (for all other capital assets), granting an agency the authority to dispose of an asset or as provided by specific statutory authority. Refer to Subsection 30.40.45.

Disposal Date - With proper authorization, the date that the agency officially relinquishes responsibility for the asset.

Inventory Control Number - The control number inscribed on, or contained on the inventory tag attached or referring to, an asset.

Location Code - The identification code of the county in which the asset is located. Refer to Subsection 30.50.20 for Schedule B for Location (County) Codes.

Manufacturer - The name of either the manufacturer or the commonly accepted trade name; if none, then vendor name.

Order Number - The number of the purchasing document used for the acquisition of the asset.

Ownership Status - An indication as to possible claims against the asset by outside parties (e.g., federal government).

Quantity - The physical count of the inventoriable items. For equipment, this number is to be expressed as whole units; for buildings, as square feet; for land, in acres to the nearest tenth, except for tidelands and shorelands which are to be expressed in front footage; and for construction in progress, as number of capital projects under construction.

Salvage Value - The estimated portion of a capital asset's cost that is recovered at the end of its service life less any disposal costs. This element is not applicable to small and attractive assets.

Serial Number - The sequential identification number assigned by the manufacturer. Do not confuse this number with the model number.

Useful Life - The estimated useful life of the capital asset in years or months. Refer to Subsection 30.50.10 for Schedule A - Capital Asset Class Codes and Useful Life Schedule. This element is not applicable to small and attractive assets.

30.40.40 Adding capital assets to the inventory

Upon receipt and acceptance of an inventoriable asset, the agency inventory officer is responsible for supervising the addition of the asset to the inventory system. This includes assigning tagging responsibilities to specific individuals as well as developing and implementing procedures to ensure that the necessary information is entered into the agency's capital asset inventory system.

30.45.10 Physical inventory frequency

Conduct physical inventories at least once every other fiscal year for all inventoriable assets except as noted below.

Due to the stationary nature of certain assets (such as land, infrastructure, buildings, improvements other than buildings, and leasehold improvements), performing a physical inventory every other fiscal year is not required.

Agencies may conduct their capital assets inventory on a revolving basis if the following conditions are met:

- Every item is subject to a physical count or verification at least once every other fiscal year.
- The inventory program is documented and active.

As an alternative to conducting a physical inventory of every inventoriable asset at least once every other year, an agency may, pursuant to Subsection 1.10.50, request OFM approval for a risk based sampling approach to a physical inventory. Requests for approval and the agency's capital asset risk assessment are to be sent to the OFM Accounting Division. Documents submitted to OFM for approval should include:

- A capital asset risk assessment that identifies the objectives and risks of the capital asset cycle;
- Analysis of the control policies and procedures surrounding agency capital asset purchases, dispositions, impairments, inventorying and financial reporting; and
- The impact of the risk assessment on the sampling approach (i.e. which assets are high risk and therefore should be tested).

30.45.20 Who should conduct and verify the physical inventory?

In order to ensure objective reporting of inventory items, a physical inventory should be performed by personnel having no direct responsibility (custody and receipt/issue authority) for assets subject to the inventory count. If it is not feasible to use such personnel for any part of the inventory, then those portions are, at least, to be tested and verified by a person with neither direct responsibility for that portion of the inventory nor supervised by the person directly responsible.

30.45.30 Physical inventory instructions

Written physical inventory instructions must be documented and distributed to each person participating in the inventory process. The instructions should describe:

- How and where to record each item,
- What information to record
- What to do when they have a question
- What procedures to follow when they finish their assignments
- What procedures to follow when equipment is located but not listed,
- The procedure by which the person counting the assets attests to the accuracy of the count, such as by signing his or her name at the bottom of each inventory page, or signing a cover page for a group of pages sorted by another method (batches, location, equipment type, etc.) and
- How to record assets not being used or in an obviously unserviceable condition. Such information is to be used to schedule repair or disposition of such assets.

30.45.40 Physical inventory reconciliations

After the physical inventory count is completed, the agency inventory officer is to conduct the reconciliation process. When all differences have been identified and explained, the inventory is considered reconciled.

Agencies should conduct the following steps during the reconciliation process:

- Search the inventory lists to determine whether inventory noted during the count as unrecorded is, in fact, listed on another portion of the inventory.
- Enter unrecorded assets into the inventory system as soon as possible after discovery.
- If a significant number of unrecorded assets are located, indicating a major problem with the asset recording procedures, the agency inventory officer is to determine why the problem is occurring and correct it.
- Conduct a search in an effort to locate missing assets. For those assets not located, inventory officers are to follow procedures outlined in Subsection 30.40.80.

After the inventory is reconciled, the agency inventory officer is to certify the reconciliation with a statement and signature that it is correct and report this to the supervisor. If the certification cannot be made, the inventory officer is to disclose that fact and the supervisor is to determine the appropriate course of action.

The Washington State Office of Financial Management, State Administrative and Accounting Manual (SAAM), Chapter 35 – Inventories, states in part:

35.10.10 Policies in this chapter are minimum standards

The policies and procedures in this chapter are the minimum requirements for inventories that state agencies must meet. An agency may maintain its inventory system in greater detail, or use

additional supporting documentation, as long as the agency meets the required minimum standards.

35.10.20 Applicability

All agencies of the state of Washington must comply with this chapter, unless otherwise exempted by statute. RCW 43.88.020 defines the term “Agency” to mean and include “every state office, officer, each institution, whether educational, correctional or other, and every department, division, board and commission, except as otherwise provided.”

Agencies may request a waiver from complying with specific requirements of this chapter.

35.10.25 Agency responsibilities

The agency head must designate in writing, one or more Agency Inventory Officers to be responsible for maintaining and safeguarding the agency’s inventories. These responsibilities include:

- Selecting appropriate inventory accounting methods and systems from acceptable alternatives (refer to Subsection 35.10.35 and Section 85.56);
- Developing and implementing policies and procedures to safeguard, control, and account for inventories;
- Defining inventory control point in the agency's written internal policies;
- Planning, conducting, and reconciling the physical inventory with inventory records;
- Documenting selected inventory valuation methods;
- Documenting physical inventory procedures; and
- Performing other duties necessary to account for and report inventories.

35.10.50 Inventory systems

a. Perpetual inventory system – A perpetual inventory system is one in which the inventory quantities and values for all purchases and issues are recorded directly in the inventory system as they occur. Perpetual inventory system balances are verified by means of periodic physical counts. A revolving physical count, where segments of inventories are counted at different times, may be used, provided all inventories are counted at least every other fiscal year.

The agency inventory officer is responsible for developing and implementing procedures for recording inventory additions as received and reductions as used.

35.10.55 Who should conduct the physical inventory?

The physical inventory, or inventory count, should be performed by persons with no direct responsibility (custody and receipt/issue authority) for the inventory. If it is not feasible to use such personnel for any part of the inventory, those parts are, at least, to be tested and verified by a person with no direct responsibility for the stock.

35.10.65 Physical inventory reconciliation and documentation

a. Perpetual inventory records must be reconciled with the physical count. The agency must investigate and explain differences, take corrective action when necessary, and adjust the accounting records per Section 85.56. When the reconciliation is complete, the agency inventory officer must certify in writing that the inventory was verified by counting and reconciliation.

2018-016

The Department of Ecology did not have adequate internal controls over and did not comply with federal requirements to ensure subrecipients of the Capitalization Grants for Clean Water State Revolving Funds program received required audits and management decisions on audit findings were issued in a timely manner.

Federal Awarding Agency: U.S. Environmental Protection Agency
Pass-Through Entity: None
CFDA Number and Title: 66.458 Capitalization Grants for Clean Water State Revolving Funds
Federal Award Number: CS-53000116; CS-53000117
Applicable Compliance Component: Subrecipient Monitoring
Known Questioned Cost Amount: None

Background

Federal capitalization grants are awarded to the State to create and maintain the Clean Water State Revolving Fund (CWSRF). In addition to the capitalization grant, CWSRF program funds came from a required state match of 20 percent of the grant, principal repayments, and interest and investment earnings. For the state fiscal year 2018 funding cycle, the Department of Ecology issued binding commitments for 40 projects totaling \$115 million from all funding sources. The purpose of the CWSRF is to provide below market rate loans and other assistance to help applicants meet the wastewater and other clean water needs of their communities.

The Department of Ecology (Department) implemented federal equivalency procedures in 2016. Equivalency refers to applying federal requirements only to an amount of CWSRF projects equal to the amount of the federal capitalization grant. The Department must track equivalency projects until disbursements are complete. The Department has identified 17 designated equivalency projects that are required to meet the single audit requirements, 10 of which were active during the audit period. Only expenditures related to the equivalency projects are considered to be made with federal funding.

Description of Condition

The Department of Ecology did not have adequate internal controls over and did not comply with federal requirements to ensure subrecipients of the CWSRF program received required audits and, if needed, management decisions on audit findings were issued in a timely manner.

We reviewed all five subrecipients that were awarded funds for the 10 active equivalency projects and found the Department did not review any of the audit reports within six months of issuance to determine if there were any findings and to issue a management decision if required.

We verified three of the audits included a finding that required the Department to issue a management decision.

We consider this internal control deficiency to be a material weakness.

This condition was not reported in the prior audit.

Cause of Condition

The Department established a spreadsheet to track subrecipient audit activity. However, the spreadsheet was not used during the audit period. No other processes were in place to monitor whether subrecipients received required audits and the Department issued a management decision, if required.

While the Department had established procedures to monitor and verify if subrecipients obtained required audits, it did not follow them. The Department had multiple staff working on different tracking spreadsheets, and it was unclear who was responsible for tracking the responses from subrecipients and notifying the CWSRF program staff.

Effect of Condition

Without establishing adequate internal controls, the Department cannot ensure all subrecipients that met the threshold for an audit complied with federal grant requirements. In addition, three subrecipients received audit findings that the Department did not issue a management decision on, as required.

Recommendations

We recommend the Department:

- Review all audits of federal equivalency projects within the required timeframes
- Follow up on all subrecipient audit findings related to those projects and issue a management decision promptly

Department's Response

Multiple people were working on the spreadsheets tracking subrecipients and it was not clear who should notify the programs of findings posted on the State Auditors Website. We have updated our procedures to clarify who notifies the Program of audit finding on subrecipients.

Auditor's Concluding Remarks

We thank the Department for its cooperation and assistance throughout the audit. We will review the status of the Department's corrective action during our next audit.

Applicable Laws and Regulations

Title 2 U.S. Code of Federal Regulations Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance) establishes the following applicable requirements:

Section 200.303 Internal controls, states in part:

The non-Federal entity must:

- (a) Establish and maintain effective internal control over the Federal award that provides reasonable assurance that the non-Federal entity is managing the Federal award in compliance with Federal statutes, regulations, and the terms and conditions of the Federal award. These internal controls should be in compliance with guidance in “Standards for Internal Control in the Federal Government” issued by the Comptroller General of the United States or the “Internal Control Integrated Framework”, issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).
- (b) Comply with Federal statutes, regulations, and the terms and conditions of the Federal awards.
- (d) Take prompt action when instances of noncompliance are identified including noncompliance identified in audit findings.

Section 200.516 Audit findings, states in part:

- (a) *Audit findings reported.* The auditor must report the following as audit findings in a schedule of findings and questioned costs:
 - (1) Significant deficiencies and material weaknesses in internal control over major programs and significant instances of abuse relating to major programs. The auditor’s determination of whether a deficiency in internal control is a significant deficiency or material weakness for the purpose of reporting an audit finding is in relation to a type of compliance requirement for a major program identified in the Compliance Supplement.
 - (2) Material noncompliance with the provisions of Federal statutes, regulations, or the terms and conditions of Federal awards related to a major program. The auditor’s determination of whether a noncompliance with the provisions of Federal statutes, regulations, or the terms and conditions of Federal awards is material for the purpose of reporting an audit finding is in relation to a type of compliance requirement for a major program identified in the compliance supplement.

Section 200.331 Requirements for pass-through entities, states in part:

- (d) Monitor the activities of the subrecipient as necessary to ensure that the subaward is used for authorized purposes, in compliance with Federal statutes, regulations, and the terms and conditions of the subaward; and that subaward performance goals are achieved. Pass-through entity monitoring of the subrecipient must include:
 - (3) Issuing a management decision for audit findings pertaining to the Federal award provided to the subrecipient from the pass-through entity as required by §200.521 Management decision.
- (f) Verify that every subrecipient is audited as required by Subpart F—Audit Requirements of this part when it is expected that the subrecipient's Federal awards expended during the respective fiscal year equaled or exceeded the threshold set forth in §200.501 Audit requirements.

The American Institute of Certified Public Accountants defines significant deficiencies and material weaknesses in internal controls over compliance in its *Codification of Statements on Auditing Standards*, section 935, Compliance Audits, as follows:

.11 For purposes of adapting GAAS to a compliance audit, the following terms have the meanings attributed as follows: ...

Deficiency in internal control over compliance. A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance on a timely basis. A deficiency in design exists when (a) a control necessary to meet the control objective is missing, or (b) an existing control is not properly designed so that, even if the control operates as designed, the control objective would not be met. A deficiency in operation exists when a properly designed control does not operate as designed or the person performing the control does not possess the necessary authority or competence to perform the control effectively.

Material weakness in internal control over compliance. A deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a compliance requirement will not be prevented, or detected and corrected, on a timely basis. In this section, a reasonable possibility exists when the likelihood of an event occurring is either reasonably possible or probable as defined as follows:

Reasonably possible. The chance of the future event or events occurring is more than remote but less than likely.

Probable. The future event or events are likely to occur.

Significant deficiency in internal control over compliance. A deficiency, or a combination of deficiencies, in internal control over compliance that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

Material noncompliance. In the absence of a definition of material noncompliance in the governmental audit requirement, a failure to follow compliance requirements or a violation of prohibitions included in the applicable compliance requirements that results in noncompliance that is quantitatively or qualitatively material, either individually or when aggregated with other noncompliance, to the affected government program.

2018-017

The Department of Ecology did not have adequate internal controls over and did not comply with reporting requirements for the Capitalization Grants for Clean Water State Revolving Funds program.

Federal Awarding Agency: U.S. Environmental Protection Agency
Pass-Through Entity: None
CFDA Number and Title: 66.458 Capitalization Grants for Clean Water State Revolving Funds
Federal Award Number: CS-53000116; CS-53000117
Applicable Compliance Component: Reporting
Known Questioned Cost Amount: None

Background

Federal capitalization grants are awarded to states to create and maintain Clean Water State Revolving Funds (CWSRF). In addition to the capitalization grant, CWSRF program funds come from a required state match of 20 percent of the grant, principal repayments, and interest and investment earnings. For the state fiscal year 2018 funding cycle, the Department of Ecology (Department) issued binding commitments for 40 projects totaling \$115 million from all funding sources. The purpose of the CWSRF is to provide below market rate loans and other assistance to assist applicants in meeting the wastewater and other clean water needs of their communities.

The Department implemented federal equivalency procedures in 2016. Equivalency refers to applying federal requirements only to an amount of CWSRF projects equal to the amount of the federal capitalization grant. The Department is required to track equivalency projects until disbursements are complete. The Department has identified 17 designated equivalency projects that are required to meet the single audit requirements, ten of which were active during the audit period. Only expenditures related to the equivalency projects are considered to be made with federal funding.

The state is required to report financial information to the grantor annually for each federal grant it has received that remains open. The Department meets this requirement by submitting the SF-425 Federal Financial Report, no later than 90 days after the end of each reporting period.

Description of Condition

The Department of Ecology did not have adequate internal controls over and did not comply with reporting requirements for the Capitalization Grants for Clean Water State Revolving Fund program.

Once the Department adopted equivalency, only expenditures related to the Designated Equivalency Projects were considered federal funds for reporting purposes. However, when filing the SF-425 report, the Department reported its financial information based on the amount of federal funds it had drawn down from the grantor. This was the proper reporting method before equivalency, but after implementation, the Department should have reported amounts related to the equivalency projects.

We consider this internal control deficiency to be a material weakness.

Cause of Condition

Although the Department implemented equivalency procedures in 2016, it did not update its internal controls and processes related to reporting. In addition, the federal grantor did not provide clear guidance as to the proper implementation of equivalency procedures as they relate to financial reporting.

Effect of Condition

During the audit period, the Department had 10 active equivalency projects that were funded by the 2016 and 2017 capitalization grants. We reviewed the associated SF-425 reports and identified the following errors:

2017 capitalization grant	Amount reported	Correct amount	Amount over or under
Federal share of expenditures	\$22,931,422	\$22,656,752	\$274,670
Federal share of unliquidated obligations ¹	\$0	\$10,097,240	(\$10,097,240)
Total federal share	\$22,931,422	\$32,753,992	(\$9,822,570)
Unobligated balance of federal funds	\$124,578	(\$9,697,992)	\$9,822,570
2016 capitalization grant	Amount reported	Correct amount	Amount over or under
Federal share of expenditures	\$23,005,531	\$79,547,338	(\$56,541,807)
Federal share of unliquidated obligations	\$275,374	\$4,071,476	(\$3,796,102)
Total federal share	\$23,280,905	\$83,618,814	(\$60,337,909)
Unobligated balance of federal funds	\$0	(\$60,383,814)	\$60,383,814

*Notes: *Unliquidated obligations* – amount of obligations incurred that have not been paid

Unobligated balance of federal funds – portion of funds authorized by the grantor that has not been obligated by the recipient

Recommendations

We recommend the Department:

- Improve its internal controls to ensure it properly reports federal equivalency expenditures on its annual report
- Contact the federal grantor for clarification, if needed

Department's Response

Ecology has requested guidance from EPA region 10 regarding amounts that should be reported on the SF-425 Federal Financial Report and the SEFA – Schedule of Federal Assistance form for “Equivalency” projects.

Auditor's Concluding Remarks

We thank the Department for its cooperation and assistance throughout the audit. We will review the status of the Department's corrective action during our next audit.

Applicable Laws and Regulations

Title 2 U.S. Code of Federal Regulations Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance) establishes the following applicable requirements:

Section 200.303 Internal controls, states in part:

The non-Federal entity must:

- (a) Establish and maintain effective internal control over the Federal award that provides reasonable assurance that the non-Federal entity is managing the Federal award in compliance with Federal statutes, regulations, and the terms and conditions of the Federal award. These internal controls should be in compliance with guidance in “Standards for Internal Control in the Federal Government” issued by the Comptroller General of the United States or the “Internal Control Integrated Framework”, issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).
- (b) Comply with Federal statutes, regulations, and the terms and conditions of the Federal awards.
- (d) Take prompt action when instances of noncompliance are identified including noncompliance identified in audit findings.

Section 200.516 Audit findings, states in part:

- (a) *Audit findings reported.* The auditor must report the following as audit findings in a schedule of findings and questioned costs:
 - (1) Significant deficiencies and material weaknesses in internal control over major programs and significant instances of abuse relating to major programs. The auditor’s determination of whether a deficiency in internal control is a significant deficiency or material weakness for the purpose of reporting an audit finding is in relation to a type of compliance requirement for a major program identified in the Compliance Supplement.
 - (2) Material noncompliance with the provisions of Federal statutes, regulations, or the terms and conditions of Federal awards related to a major program. The auditor’s determination of whether a noncompliance with the provisions of Federal statutes, regulations, or the terms and conditions of Federal awards is material for the purpose of reporting an audit finding is in relation to a type of compliance requirement for a major program identified in the compliance supplement.

Title 2 U.S. Code of Federal Regulations Part 200, Appendix XI, Compliance Supplement 2017, Part 3-Compliance Requirements, states in part:

Section L. Reporting, states in part:

Financial Reporting

Recipients should use the standard financial reporting forms or such other forms as may be authorized by OMB (approval is indicated by an OMB paperwork control number on the form). Each recipient must report program outlays and program income on a cash or accrual basis, as prescribed by the Federal awarding agency. If the Federal awarding agency requires reporting of accrual information and the recipient’s accounting records are not normally

maintained on the accrual basis, the recipient is not required to convert its accounting system to an accrual basis but may develop such accrual information through analysis of available documentation. The Federal awarding agency may accept identical information from the recipient in machine-readable format, computer printouts, or electronic outputs in lieu of the prescribed formats.

The financial reporting requirements for subrecipients are as specified by the pass-through entity. In many cases, these will be the same as or similar to the following requirements for recipients.

The standard financial reporting forms are as follows:

3. *Federal Financial Report (FFR) (SF-425/SF-425A (OMB No. 0348-0061))*. Recipients use the FFR as a standardized format to report expenditures under Federal awards, as well as, when applicable, cash status (Lines 10.a, 10.b, and 10c). References to this report include its applicability as both an expenditure and a cash status report unless otherwise indicated.

Section IV, Other Information, states:

Equivalency

To achieve consistency in meeting program requirements and eliminate the possibility of over-reporting information under the Federal Funding Accountability and Transparency Act (Transparency Act), State CWSRF programs must use the same group of loans for the purpose of meeting Federal cross-cutting, single audit, procurement, and Transparency Act reporting requirements.

The American Institute of Certified Public Accountants defines significant deficiencies and material weaknesses in internal controls over compliance in its *Codification of Statements on Auditing Standards*, section 935, Compliance Audits, as follows:

- .11 For purposes of adapting GAAS to a compliance audit, the following terms have the meanings attributed as follows: ...

Deficiency in internal control over compliance. A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance on a timely basis. A deficiency in design exists when (a) a control necessary to meet the control objective is missing, or (b) an existing control is not properly designed so that, even if the control operates as designed, the control objective would not be met. A deficiency in operation exists when a properly designed control does not operate as designed or the person performing the control does not possess the necessary authority or competence to perform the control effectively.

Material weakness in internal control over compliance. A deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a compliance requirement will not be prevented, or

detected and corrected, on a timely basis. In this section, a reasonable possibility exists when the likelihood of an event occurring is either reasonably possible or probable as defined as follows:

Reasonably possible. The chance of the future event or events occurring is more than remote but less than likely.

Probable. The future event or events are likely to occur.

Significant deficiency in internal control over compliance. A deficiency, or a combination of deficiencies, in internal control over compliance that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

Material noncompliance. In the absence of a definition of material noncompliance in the governmental audit requirement, a failure to follow compliance requirements or a violation of prohibitions included in the applicable compliance requirements that results in noncompliance that is quantitatively or qualitatively material, either individually or when aggregated with other noncompliance, to the affected government program.

2018-018

The Department of Services for the Blind did not have adequate internal controls over federal requirements to determine client eligibility for the Vocational Rehabilitation program within a reasonable time period.

Federal Awarding Agency: U.S Department of Education
Pass-Through Entity: None
CFDA Number and Title: 84.126 Rehabilitation Services – Vocational Rehabilitation Grants to States.
Federal Award Number: H126A170072, H126A1800072
Applicable Compliance Component: Eligibility
Known Questioned Cost Amount: None

Background

The Department of Services for the Blind’s (Department) Vocational Rehabilitation program provides services for individuals who are blind, are going blind or have low vision so that such individuals may prepare for and engage in gainful employment. These services are primarily funded by federal Vocational Rehabilitation grants.

The Department operates and administers the program in accordance with federal laws and regulations, as well as with a State Plan that is approved every fiscal year. In most cases, client eligibility must be determined within a reasonable time not to exceed 60 days. There are two exceptions to the 60-day requirement:

- An exceptional and unforeseen circumstance occurred beyond the Department’s control, and the individual agreed to a specific time extension.
- The Department is assessing the client’s ability to perform in work situations through trial work experience.

If either of these exceptions is met, Department staff must document the determination in its case management system. In the case of an unforeseen circumstance, Departmental procedures require staff to enter the following information into the case management system:

- Clear justification for the exception
- An outline of the action needed to complete the determination
- How the individual was informed of the need for an extension
- That the individual accepted the justification and agreed to an extension

The system must be updated to address the above four points every 30 days after the initial entry until either the individual is found eligible or the case is closed.

To ensure eligibility decisions are made within 60 days, Department staff use a dashboard feature from its case management system to identify clients who are nearing or have exceeded the deadline. These reports are visible to counselor supervisors, who discuss timelines with staff.

In prior audits, we reported the Department did not have adequate internal controls over, and was not compliant with, federal requirements to determine client eligibility for the Vocational Rehabilitation program within a reasonable time.

The prior finding numbers were 2017-007 and 2016-009.

Description of Condition

The Department of Services for the Blind did not have adequate internal controls over federal requirements to ensure eligibility determinations were made within 60 days as required.

The Department gave us case management system reports of all clients who were determined to be eligible during the audit period. The reports showed 27 of 390 determinations occurred after the 60-day limit. We examined all 27 of these eligibility determinations and found 13 cases (48 percent) in which the Department's internal controls failed, resulting in the eligibility determination occurring after the 60-day limit without evidence the required criteria for an extension were met.

For these 13 cases, we specifically found:

- Seven cases in which no exceptional or unforeseen circumstance for the delay was documented
- Six cases in which there was no documentation to show the client agreed to a specific extension
- Six cases in which no extension was documented before the deadline
- One case in which an extension letter was sent but no determination was documented in the case management system

We also examined 28 eligibility determinations, selected using a statistically valid random sampling method, that were documented as having been completed in under 60 days and found no instances of noncompliance. We determined the internal control weakness caused 3 percent (13 of 390) of the cases during the audit period to occur after the 60-day limit without evidence the extension was proper.

We consider these internal control deficiencies to be a significant deficiency.

Cause of Condition

The Department has not defined what unforeseen or exceptional circumstances are and therefore cannot adequately determine what documentation should be maintained to justify an overdue extension. Additionally, while the dashboard queue significantly reduced the number of eligibility determinations that did not meet the 60-day requirement, management has not implemented a formal confirmation or review process to ensure an exceptional or unforeseen circumstance is documented and that the client agreed to an extension.

Effect of Condition

Because it has not implemented adequate internal controls, the Department is not always making timely eligibility decisions in accordance with federal law. We identified 13 clients who were not determined to be eligible within federally required timelines. This condition could lead to ineligible clients receiving services and puts the Department at risk the federal grantor will withhold funds.

Recommendations

We recommend the Department:

- Improve its internal controls to ensure eligibility determinations are made promptly
- Define exceptional and unforeseen circumstances so proper documentation can be maintained
- Ensure that exceptional and unforeseen circumstances are properly documented
- Ensure that extensions are supported with a client agreement that includes a specific period of time
- Ensure supervisory reviews are effective and properly documented

Department's Response

The department continues to improve internal controls for determining eligibility within the 60 day requirement and documenting a justification when a delay is necessary.

The number of delayed eligibilities continue to decline. For SFY 2018, 3% of eligibility determinations were delayed compared to 8.3% in SFY 2017 and 12.5% in SFY 2016. This improvement is due to ongoing coaching and monitoring. It should be noted that a significant number of the 3% of delayed eligibilities were delayed by 1- 3 days. This was often an error in calculating the 60 days from date of application and adding 60, however, this resulted in 61 to 63 days after application.

The department will continue to coach staff about eligibility requirements and accurately calculating the 60 days.

Auditor's Concluding Remarks

We thank the Department for its cooperation and assistance throughout the audit. We will review the status of the Department's corrective action during our next audit.

Applicable Laws and Regulations

Title 2 U.S. Code of Federal Regulations Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance) establishes the following applicable requirements:

Section 200.303 Internal controls, states in part:

The non-Federal entity must:

- (a) Establish and maintain effective internal control over the Federal award that provides reasonable assurance that the non-Federal entity is managing the Federal award in compliance with Federal statutes, regulations, and the terms and conditions of the Federal award. These internal controls should be in compliance with guidance in “Standards for Internal Control in the Federal Government” issued by the Comptroller General of the United States or the “Internal Control Integrated Framework”, issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).

Section 200.516 Audit findings, states in part:

- (a) *Audit findings reported.* The auditor must report the following as audit findings in a schedule of findings and questioned costs:
 - (1) Significant deficiencies and material weaknesses in internal control over major programs and significant instances of abuse relating to major programs. The auditor’s determination of whether a deficiency in internal control is a significant deficiency or material weakness for the purpose of reporting an audit finding is in relation to a type of compliance requirement for a major program identified in the Compliance Supplement.

The American Institute of Certified Public Accountants defines significant deficiencies and material weaknesses in internal controls over compliance in its *Codification of Statements on Auditing Standards*, section 935, Compliance Audits, as follows:

.11 For purposes of adapting GAAS to a compliance audit, the following terms have the meanings attributed as follows: ...

Deficiency in internal control over compliance. A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance on a timely basis. A deficiency in design exists when (a) a control necessary to meet the control objective is missing, or (b) an existing control is not properly designed so that, even if the control operates as designed, the control objective would not be met. A deficiency in operation exists when a properly designed control does not operate as designed or the person performing the control does not possess the necessary authority or competence to perform the control effectively.

Material weakness in internal control over compliance. A deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a compliance requirement will not be prevented, or detected and corrected, on a timely basis. In this section, a reasonable possibility exists when the likelihood of an event occurring is either reasonably possible or probable as defined as follows:

Reasonably possible. The chance of the future event or events occurring is more than remote but less than likely.

Probable. The future event or events are likely to occur.

Significant deficiency in internal control over compliance. A deficiency, or a combination of deficiencies, in internal control over compliance that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

29 United States Code section 722. Eligibility and individual plan for employment, states in part:

(a) Eligibility

(6) Timeframe for making an eligibility determination

The designated State unit shall determine whether an individual is eligible for vocational rehabilitation services under this subchapter within a reasonable period of time, not to exceed 60 days, after the individual has submitted an application for the services unless—

- (A) exceptional and unforeseen circumstances beyond the control of the designated State unit preclude making an eligibility determination within 60 days and the designated State unit and the individual agree to a specific extension of time; or
- (B) the designated State unit is exploring an individual's abilities, capabilities, and capacity to perform in work situations under paragraph (2)(B).

Washington Administrative Code 67-25-025 Eligibility for services, states:

- (1) The department shall determine whether an individual is eligible for vocational rehabilitation services within sixty days after receipt of an application for services, unless, exceptional and unforeseen circumstances beyond the control of the department preclude completion of the determination within sixty days, in which case, the department will notify the applicant.
- (2) The applicant must agree to an extension of eligibility determination or, must agree to participate in trial work experience or extended evaluation in accordance with WAC 67-25-065 and 67-25-070. If the applicant does not agree to an extension of the eligibility determination or does not agree to participate in trial work experience or extended evaluation, the applicant will be determined ineligible for vocational rehabilitation services and the case service record will be closed in accordance with WAC 67-25-055.

Washington State Department of Services for the Blind Vocational Rehabilitation Procedures states:

3. ELIGIBILITY (WAC 67-25-025) Eligibility Timelines

The Rehabilitation Act requires that eligibility determination be made within 60 days after receiving an application. The only exception is if unforeseen circumstances beyond the control of the VR Team prevent completion of the determination within 60 days. Case note E60 “Eligibility Determination over 60 Days” is used to document this exception and must:

- Provide clear justification for the exception;
- Outline needed action to complete the determination;
- Indicate how the individual was informed of the need for an extension; and
- Indicate that the individual accepts the justification and agrees to an extension.

Case note E60 must be completed to address the above four points (ideally as bullet points) every 30 days after the initial entry until the individual is found eligible, or the case is closed.

2018-019

The Department of Services for the Blind did not have adequate internal controls over reporting requirements for the Vocational Rehabilitation Grant.

Federal Awarding Agency: U.S. Department of Education
Pass-Through Entity: None
CFDA Number and Title: 84.126 Rehabilitation Services – Vocational Rehabilitation Grants to States
Federal Award Number: H126A1700072, H126A1800072,
Applicable Compliance Component: Reporting
Known Questioned Cost Amount: None

Background

The Department of Services for the Blind’s Vocational Rehabilitation program provides services for people who are blind, are going blind or have low vision so that they may prepare for and engage in gainful employment. These services are primarily funded by the Vocational Rehabilitation (VR) Grant.

The Department is required to submit a program cost report (RSA-2), which is used to report expenditures for particular services, numbers of clients served, numbers of staff and amounts transferred in and out of the program. This information is used by the grantor to evaluate and monitor the financial performance and achievements of state’s VR agencies. The report must be completed annually and is due by December 31 after the close of the federal fiscal year and must include information about all open grant awards.

In the prior audit, we reported the Department did not establish adequate internal controls over, and did not comply with, federal reporting requirements. The prior finding number was 2017-010.

Description of Condition

We found the Department did not have adequate internal controls to ensure its federal program cost report was prepared accurately during the audit period. Specifically, the Department did not perform a secondary review of the RSA-2 report and the accounting data supporting it before submitting the report to the federal grantor.

We consider this control deficiency to be a material weakness.

Cause of Condition

The Department experienced staff changes in the positions that create and review the reports. After the staffing changes, the Department believed it no longer had staff with the necessary knowledge to perform a secondary review.

Effect of Condition

By not establishing adequate internal controls, the Department is at a higher risk of not detecting errors and misreporting information to the grantor.

Recommendation

We recommend the Department improve its internal controls by performing a secondary review of its RSA-2 reports.

Department's Response

The Department of Services for the Blind continues to experience staff turnover in the fiscal unit. The Department recently hired a consultant to assist with an organization plan that will meet the requirements of a secondary review. It is anticipated the organizational plan and hiring of required staff will be completed by 6/30/2019.

Auditor's Concluding Remarks

We thank the Department for its cooperation and assistance throughout the audit. We will review the status of the Department's corrective action during our next audit.

Applicable Laws and Regulations

Title 2 U.S. Code of Federal Regulations Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance) establishes the following applicable requirements:

Section 200.303 Internal controls, states in part:

The non-Federal entity must:

- (a) Establish and maintain effective internal control over the Federal award that provides reasonable assurance that the non-Federal entity is managing the Federal award in compliance with Federal statutes, regulations, and the terms and conditions of the Federal award. These internal controls should be in compliance with guidance in "Standards for Internal Control in the Federal Government" issued by the Comptroller General of the United States or the "Internal Control Integrated Framework", issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).

Section 200.516 Audit findings, states in part:

- (a) *Audit findings reported.* The auditor must report the following as audit findings in a schedule of findings and questioned costs:
 - (1) Significant deficiencies and material weaknesses in internal control over major programs and significant instances of abuse relating to major programs. The auditor's determination of whether a deficiency in internal control is a significant deficiency or material weakness for the purpose of reporting an audit finding is in

relation to a type of compliance requirement for a major program identified in the Compliance Supplement.

The American Institute of Certified Public Accountants defines significant deficiencies and material weaknesses in internal controls over compliance in its *Codification of Statements on Auditing Standards*, section 935, Compliance Audits, as follows:

.11 For purposes of adapting GAAS to a compliance audit, the following terms have the meanings attributed as follows: ...

Deficiency in internal control over compliance. A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance on a timely basis. A deficiency in design exists when (a) a control necessary to meet the control objective is missing, or (b) an existing control is not properly designed so that, even if the control operates as designed, the control objective would not be met. A deficiency in operation exists when a properly designed control does not operate as designed or the person performing the control does not possess the necessary authority or competence to perform the control effectively.

Material weakness in internal control over compliance. A deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a compliance requirement will not be prevented, or detected and corrected, on a timely basis. In this section, a reasonable possibility exists when the likelihood of an event occurring is either reasonably possible or probable as defined as follows:

Reasonably possible. The chance of the future event or events occurring is more than remote but less than likely.

Probable. The future event or events are likely to occur.

Significant deficiency in internal control over compliance. A deficiency, or a combination of deficiencies, in internal control over compliance that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

2018-020

The Department of Services for the Blind did not have adequate internal controls over and was not compliant with requirements to ensure cash draws were accurate and timely for the Vocational Rehabilitation program.

Federal Awarding Agency: U.S Department of Education
Pass-Through Entity: None
CFDA Number and Title: 84.126 Rehabilitation Services – Vocational Rehabilitation Grants to States.
Federal Award Number: H126A1700072, H126A1800072
Applicable Compliance Component: Cash Management
Known Questioned Cost Amount: None

Background

The Department of Services for the Blind’s (Department) Vocational Rehabilitation program provides services for individuals who are blind, are going blind or have low vision so that such individuals may prepare for and engage in gainful employment. These services are primarily funded by the Vocational Rehabilitation Grant.

The Department operates the program in accordance with federal laws and regulations, as well as with a Cash Management Improvement Act (CMIA) agreement between the State and the U.S. Department of the Treasury. The CMIA agreement requires the Department to draw funds from the federal grantor twice a month on a reimbursement basis. At times, multiple grants are open so more than one draw may be made on the same date.

The Department established a procedure that requires a secondary review before funds are drawn to ensure the process occurs properly. The review is performed by another manager and is supposed to happen before the funds are drawn.

In the prior audit, we reported the Department did not have adequate internal controls to ensure cash draws were accurate for the Vocational Rehabilitation program. The prior finding number was 2017-008.

Description of Condition

The Department did not have adequate internal controls to ensure cash draws were accurate and timely. For six of the 24 grant months (25 percent) when the Department drew down federal funds, the amount supported in the Department’s accounting system did not match what was requested from the grantor. The Department over-drew the grant for four months (totaling \$600,000) and under-drew for two months (totaling \$600,000).

We also found:

- No secondary review occurred in May or June 2018.
- Four draws (17 percent) were not requested at the proper time, as required by the CMIA.

We consider these control deficiencies to be a material weakness.

Cause of Condition

The Department had turnover in staff who oversaw the draw process. Management did not ensure availability of backup staff with expertise in how to process and review the grant draws.

Effect of Condition

By not establishing adequate internal controls, the Department cannot ensure that draw amounts they requested were accurate and timely. The Department drew funds that were not supported by expenditures and performed draws late.

Recommendation

We recommend the Department:

- Improve internal controls to ensure cash draws are performed accurately and in accordance with the state's CMIA agreement
- Ensure secondary reviews are performed by staff who understand federal grant requirements
- Provide adequate training to staff to ensure federal draws are performed in a timely manner.

Department's Response

The Department had experienced staff turnover in the fiscal unit that affected the level of oversight over the federal draw process. In response to prior audit findings, the Department had implemented corrective actions to address the audit recommendations. However, the Department continues to experience staff turnover in the positions that perform federal draws.

As of December 2018, the Department hired a consultant to:

- *Assist with an organizational plan for the fiscal unit.*
- *Strengthen internal controls over the federal draw process to include a secondary review.*

The Department anticipates that the organizational plan and hiring of required staff will be completed by June 2019.

Auditor's Concluding Remarks

We thank the Department for its cooperation and assistance throughout the audit. We will review the status of the Department's corrective action during our next audit.

Applicable Laws and Regulations

Title 2 U.S. Code of Federal Regulations Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance) establishes the following applicable requirements:

Section 200.303 Internal controls, states in part:

The non-Federal entity must:

- (a) Establish and maintain effective internal control over the Federal award that provides reasonable assurance that the non-Federal entity is managing the Federal award in compliance with Federal statutes, regulations, and the terms and conditions of the Federal award. These internal controls should be in compliance with guidance in “Standards for Internal Control in the Federal Government” issued by the Comptroller General of the United States or the “Internal Control Integrated Framework”, issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).
- (b) Comply with Federal statutes, regulations, and the terms and conditions of the Federal awards.
- (d) Take prompt action when instances of noncompliance are identified including noncompliance identified in audit findings.

Section 200.516 Audit findings, states in part:

- (a) *Audit findings reported.* The auditor must report the following as audit findings in a schedule of findings and questioned costs:
 - (1) Significant deficiencies and material weaknesses in internal control over major programs and significant instances of abuse relating to major programs. The auditor’s determination of whether a deficiency in internal control is a significant deficiency or material weakness for the purpose of reporting an audit finding is in relation to a type of compliance requirement for a major program identified in the Compliance Supplement.
 - (2) Material noncompliance with the provisions of Federal statutes, regulations, or the terms and conditions of Federal awards related to a major program. The auditor’s determination of whether a noncompliance with the provisions of Federal statutes, regulations, or the terms and conditions of Federal awards is material for the purpose of reporting an audit finding is in relation to a type of compliance requirement for a major program identified in the compliance supplement.

The American Institute of Certified Public Accountants defines significant deficiencies and material weaknesses in internal controls over compliance in its *Codification of Statements on Auditing Standards*, section 935, Compliance Audits, as follows:

.11 For purposes of adapting GAAS to a compliance audit, the following terms have the meanings attributed as follows: ...

Deficiency in internal control over compliance. A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to

prevent, or detect and correct, noncompliance on a timely basis. A deficiency in design exists when (a) a control necessary to meet the control objective is missing, or (b) an existing control is not properly designed so that, even if the control operates as designed, the control objective would not be met. A deficiency in operation exists when a properly designed control does not operate as designed or the person performing the control does not possess the necessary authority or competence to perform the control effectively.

Material weakness in internal control over compliance. A deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a compliance requirement will not be prevented, or detected and corrected, on a timely basis. In this section, a reasonable possibility exists when the likelihood of an event occurring is either reasonably possible or probable as defined as follows:

Reasonably possible. The chance of the future event or events occurring is more than remote but less than likely.

Probable. The future event or events are likely to occur.

Significant deficiency in internal control over compliance. A deficiency, or a combination of deficiencies, in internal control over compliance that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

Material noncompliance. In the absence of a definition of material noncompliance in the governmental audit requirement, a failure to follow compliance requirements or a violation of prohibitions included in the applicable compliance requirements that results in noncompliance that is quantitatively or qualitatively material, either individually or when aggregated with other noncompliance, to the affected government program.

Cash Management Improvement Act Agreement between The State of Washington and The Secretary of the Treasury, United States Department of the Treasury, states, in part:

84.126 Rehabilitation Services -- Vocational Rehabilitation Grants to States

Recipient: 315---Department of Services for the Blind---DSB

% of Funds Agency Receives: 16.11

Component: Payments made to clients and to support clients, payroll, and administrative costs

Technique: Modified Direct Program Costs -Admin, Payroll, Payments to Providers (ACH Drawdown on Payroll Cycle) Average Day of Clearance: 0 Days

Modified Direct Program Costs - Admin, Payroll, Payments to Providers (ACH Drawdown on Payroll Cycle)

The State shall request funds for all direct administrative costs and/or payroll costs, and/or payments made to providers and to support providers. The request shall be made in accordance with the appropriate Federal agency cut-off time specified in Exhibit I. The amount of the funds requested shall be based on the amount of expenditures recorded for direct administrative costs and/or payroll costs and/or payments made to providers or to support providers since the last request for funds. The State payroll cycle is payday twice a month. Draws made day before payday are for deposit on payday. The draw request will be made in

accordance with cut-off time in Exhibit 1. The amount of the funds requested shall be based on the amount of expenditures recorded for direct administrative costs and/or payroll costs and/or payments made to providers or to support providers since the last request for funds. This funding technique is interest neutral.

2018-021

The Department of Social and Health Services did not have adequate internal controls over and was not compliant with federal requirements to determine client eligibility for the Vocational Rehabilitation program within a reasonable period of time.

Federal Awarding Agency: U.S Department of Education
Pass-Through Entity: None
CFDA Number and Title: 84.126 Rehabilitation Services – Vocational Rehabilitation Grants to States.
Federal Award Number: H126A160071, H126A170071, H126A180071
Applicable Compliance Component: Eligibility
Known Questioned Cost Amount: None

Background

The Department of Social and Health Services' Division of Vocational Rehabilitation (Department) provides employment services and counseling to individuals with disabilities who want to work but experience barriers to work because of a physical, sensory and/or mental disability. These services are primarily funded by the Vocational Rehabilitation Grant.

The Department operates and administers the program in accordance with federal laws and regulations, as well as with a State Plan that is approved every fiscal year. To be eligible for service, an individual must undergo an assessment to determine eligibility, which includes obtaining medical documentation to support the person's disability. The applicant must also have an employment goal and be able to work.

In most cases, client eligibility must be determined within a reasonable time not to exceed 60 days. There are two exceptions to the 60-day requirement:

- An exceptional and unforeseen circumstance occurred beyond the Department's control, and the individual agreed to a specific time extension.
- The Department is assessing the client's ability to perform in work situations through trial work experience.

If either of these exceptions is met, Department staff must document the determination in its case management system. In the case of an unforeseen circumstance, Departmental procedures require staff to document the following information in the case management system:

- Clear justification for the exception
- An outline of the action needed to complete the determination
- How the individual was informed of the need for an extension
- That the individual accepted the justification and agreed to an extension

To ensure eligibility decisions are made within 60 days, Department staff use a queue feature from its case management system to identify clients who are nearing or have exceeded the deadline. The queue is visible to counselor's supervisors, who discuss timelines with staff. The client will remain in the queue until determined eligible or closed in the case management system.

In prior audits, we reported the Department did not have adequate internal controls over, and was not compliant with, federal requirements to determine client eligibility for the Vocational Rehabilitation program within a reasonable time. The prior finding numbers were 2017-013 and 2016-012.

Description of Condition

The Department did not have adequate internal controls over federal requirements to ensure eligibility determinations were made within 60 days as required.

The Department provided us case management system reports of all 7,215 clients who were determined eligible during the audit period. We divided these clients into two different populations: those who were determined eligible within 60 days (6,374), and those who were not (841). We used a statistical sampling method to randomly select and examine 59 of the determinations that were made within 60 days, and 57 that were not. For those determinations made under 60 days, we identified one case where the Department did not have a signed application from the client. For the determinations over 60 days, we found 48 cases (84 percent) in which the eligibility determination occurred after the 60-day limit without evidence the required criteria for an extension were met.

For these 48 cases, we found:

- 37 cases in which no exceptional and unforeseen circumstance for the delay was documented
- 40 cases in which there was no documentation to show the client agreed to a specific extension
- 34 cases in which no extension was documented before the deadline
- 29 cases in which the client was not determined eligible by the new deadline.

We also determined the Department's new queue feature did not ensure more timely case completion. During the last audit, we determined 8 percent of determinations were made after 60 days, while this year that rose to almost 12 percent.

We consider these internal control deficiencies to be a material weakness.

Cause of Condition

The Department had not defined what unforeseen and exceptional circumstances are and therefore could not adequately determine what documentation should be maintained to justify an overdue extension. Additionally, management did not monitor the queue, nor implement a formal confirmation or review process, to ensure an exceptional and unforeseen circumstance is documented and that the client agreed to an extension before the 60-day limit was reached.

Effect of Condition

Because it has not implemented adequate internal controls, the Department is not always making timely eligibility decisions in accordance with federal law.

Recommendation

We recommend the Department:

- Improve its internal controls to ensure eligibility determinations are made promptly
- Define exceptional and unforeseen circumstances so proper documentation can be maintained
- Ensure that exceptional and unforeseen circumstances are properly documented
- Ensure that extensions are supported with a client agreement that includes a specific period of time
- Ensure supervisory reviews are effective and properly documented

Department's Response

The Department concurs with the finding.

The Department has implemented additional procedural guidance and enhanced management reports aimed at ensuring full compliance with federal requirements that client eligibility for DVR services must be determined within 60-days after application, unless extended to a longer timeframe by signed agreement between the VR Counselor and client. In addition, management reports and coaching tools have been enhanced to support supervisory oversight and monitoring of compliance with eligibility timelines and required procedures.

This finding demonstrates that further action is needed to ensure that service delivery practices fully comply with federal requirements as well as departmental policies and procedures for the determination of client eligibility.

Corrective actions will be implemented to achieve more intensive supervisory review and follow-up to monitor eligibility determinations. Additional guidance will be provided that clearly defines exceptional and unforeseen circumstances that merit an extension of timeframe, and further training will be provided to VR Counselors and VR Supervisors.

Auditor's Concluding Remarks

We thank the Department for its cooperation and assistance throughout the audit. We will review the status of the Department's corrective action during our next audit.

Applicable Laws and Regulations

Title 2 U.S. Code of Federal Regulations Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance) establishes the following applicable requirements:

Section 200.303 Internal controls, states in part:

The non-Federal entity must:

- (a) Establish and maintain effective internal control over the Federal award that provides reasonable assurance that the non-Federal entity is managing the Federal award in compliance with Federal statutes, regulations, and the terms and conditions of the Federal award. These internal controls should be in compliance with guidance in “Standards for Internal Control in the Federal Government” issued by the Comptroller General of the United States or the “Internal Control Integrated Framework”, issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).
- (b) Comply with Federal statutes, regulations, and the terms and conditions of the Federal awards.
- (d) Take prompt action when instances of noncompliance are identified including noncompliance identified in audit findings.

Section 200.516 Audit findings, states in part:

- (a) *Audit findings reported.* The auditor must report the following as audit findings in a schedule of findings and questioned costs:
 - (1) Significant deficiencies and material weaknesses in internal control over major programs and significant instances of abuse relating to major programs. The auditor’s determination of whether a deficiency in internal control is a significant deficiency or material weakness for the purpose of reporting an audit finding is in relation to a type of compliance requirement for a major program identified in the Compliance Supplement.
 - (2) Material noncompliance with the provisions of Federal statutes, regulations, or the terms and conditions of Federal awards related to a major program. The auditor’s determination of whether a noncompliance with the provisions of Federal statutes, regulations, or the terms and conditions of Federal awards is material for the purpose of reporting an audit finding is in relation to a type of compliance requirement for a major program identified in the compliance supplement.

The American Institute of Certified Public Accountants defines significant deficiencies and material weaknesses in internal controls over compliance in its *Codification of Statements on Auditing Standards*, section 935, Compliance Audits, as follows:

.11 For purposes of adapting GAAS to a compliance audit, the following terms have the meanings attributed as follows: ...

Deficiency in internal control over compliance. A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow

management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance on a timely basis. A deficiency in design exists when (a) a control necessary to meet the control objective is missing, or (b) an existing control is not properly designed so that, even if the control operates as designed, the control objective would not be met. A deficiency in operation exists when a properly designed control does not operate as designed or the person performing the control does not possess the necessary authority or competence to perform the control effectively.

Material weakness in internal control over compliance. A deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a compliance requirement will not be prevented, or detected and corrected, on a timely basis. In this section, a reasonable possibility exists when the likelihood of an event occurring is either reasonably possible or probable as defined as follows:

Reasonably possible. The chance of the future event or events occurring is more than remote but less than likely.

Probable. The future event or events are likely to occur.

Significant deficiency in internal control over compliance. A deficiency, or a combination of deficiencies, in internal control over compliance that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

Material noncompliance. In the absence of a definition of material noncompliance in the governmental audit requirement, a failure to follow compliance requirements or a violation of prohibitions included in the applicable compliance requirements that results in noncompliance that is quantitatively or qualitatively material, either individually or when aggregated with other noncompliance, to the affected government program.

29 U.S. Code section 722. Eligibility and individual plan for employment, states in part:

(a) Eligibility

(1) Criterion for eligibility

An individual is eligible for assistance under this subchapter if the individual—

(A) has undergone an assessment for determining eligibility and vocational rehabilitation needs and as a result has been determined to be an individual with a disability under section 705(20)(A) of this title; and

(B) requires vocational rehabilitation services to prepare for, secure, retain, advance in, or regain employment that is consistent with the individual's strengths, resources, priorities, concerns, abilities, capabilities, interests, and informed choice.

(3) Presumption of eligibility

(A) In general

For purposes of this section, an individual who has a disability or is blind as determined pursuant to title II or title XVI of the Social Security Act (42 U.S.C. 401 et seq. and 1381 et seq.) shall be—

- (i) considered to be an individual with a significant disability under section 705(21)(A) of this title; and
- (ii) presumed to be eligible for vocational rehabilitation services under this subchapter (provided that the individual intends to achieve an employment outcome consistent with the unique strengths, resources, priorities, concerns, abilities, capabilities, interests, and informed choice of the individual) unless the designated State unit involved can demonstrate by clear and convincing evidence that such individual is incapable of benefiting in terms of an employment outcome due to the severity of the individual's disability (as of the date of the determination).

(6) Timeframe for making an eligibility determination

The designated State unit shall determine whether an individual is eligible for vocational rehabilitation services under this subchapter within a reasonable period of time, not to exceed 60 days, after the individual has submitted an application for the services unless—

- (A) exceptional and unforeseen circumstances beyond the control of the designated State unit preclude making an eligibility determination within 60 days and the designated State unit and the individual agree to a specific extension of time; or
- (B) the designated State unit is exploring an individual's abilities, capabilities, and capacity to perform in work situations under paragraph (2)(B).

2018-022

The Department of Social and Health Services did not have adequate internal controls over, and was not compliant with, federal requirements to establish timely individual plans of employment for Vocational Rehabilitation program clients.

Federal Awarding Agency: Department of Education
Pass-Through Entity: None
CFDA Number and Title: 84.126 Rehabilitation Services – Vocational Rehabilitation Grants to States
Federal Award Number: H126A160071, H126A170071, H126A180071
Applicable Compliance Component: Special Tests and Provisions – Completion of IPEs
Known Questioned Cost Amount: None

Background

The Department of Social and Health Services' Division of Vocational Rehabilitation (Department) provides employment services and counseling to individuals with disabilities who want to work but experience barriers to work because of a physical, sensory, and/or mental disability. A DVR counselor works with each person to develop a customized plan of services designed to help them reach their employment goal. These services are primarily funded by the Vocational Rehabilitation Grant.

The Department operates and administers the program in accordance with federal laws and regulations, as well as with a State Plan that is approved every fiscal year. It is responsible for ensuring that, once an individual is determined eligible, an Individual Plan for Employment (IPE) is created as soon as possible, but no later than 90 days after their eligibility determination date. The

IPE's creation can extend past 90 days only if the Department and the individual agree to an extension with a specific date by which it must be completed. When this happens, Department staff must document the extension in the Department's case management system.

The Department requires that counselors send a letter to the client informing them of the need for an extension and the date by which the counselors believe they can create an IPE. The client is then required to sign the letter and return it to the Department to indicate that they agree to the extension. The Department also requires that the counselor and the client sign and date the completed IPE, within the 90-day limit, to indicate that they agree to the plan that was developed. Without both signatures, the IPE is not binding.

To ensure IPEs are entered into within 90 days, Department staff use a dashboard feature from the Department's case management system to identify clients who are nearing or have exceeded the deadline. These reports are visible to supervisors, who discuss timelines with staff.

In the prior two audits, we reported the Department did not have adequate internal controls over, and was not compliant with, federal requirements to establish timely IPEs for program clients. The prior finding numbers were 2017-012 and 2016-011.

Description of Condition

The Department did not have adequate internal controls over, and was not compliant with, federal requirements to establish timely IPEs for Vocational Rehabilitation program clients.

The Department gave us case management system reports of all clients who agreed or should have agreed to an IPE during the audit period, or had their case closed. The reports showed 6,550 of 10,719 IPEs exceeded the 90-day limit. We used a statistically valid random sampling method to random select 59 cases. We examined the Department's records and found:

- 18 cases (31 percent) when the Department could not provide evidence the client agreed to the extension
- 11 cases (20 percent) when the extension was not completed in a timely manner
- Six cases (10 percent) when an extension was properly agreed upon, but the client did not enter into an IPE or have the case closed before the new deadline

We also examined 59 of 4,169 clients, selected using a statistically valid random sampling method, who the case management system reports indicated entered into IPE within the 90-day limit. We found one case (1.7 percent) when the IPE date did not match the date in the case management system and the 90-day limit was exceeded.

We consider these internal control deficiencies to be a material weakness.

Cause of Condition

The Department did not have an adequate review process to ensure counselors followed Department policy and that documentation was maintained. While the case management system provides counselors and supervisors daily reminders about cases approaching the 90-day limit, there is no guidance on how much review supervisors are to perform.

Effect of Condition

Because it has not established adequate internal controls, the Department does not always make timely IPE determinations in accordance with federal law. The Department faces increased risk of not providing services to eligible clients in a timely manner.

Based on our statistically valid, random samples, we estimate the Department did not establish a timely IPE, or lacked the documentation to support that it did, for 3,552 of the 6,550 clients the case management system identified as exceeding the 90-day limit.

Recommendations

We recommend the Department improve its internal controls to ensure:

- Documentation is maintained to show IPEs were properly completed.
- IPEs are created in a timely manner
- Extensions are agreed upon by the client and are properly documented
- Both counselors and clients approve the completed IPEs

Department's Response

The Department concurs with the finding.

The Department has implemented additional procedural guidance and enhanced management reports aimed at ensuring full compliance with federal requirements that a client's IPE must be developed within 90-days after their date of eligibility, unless extended to a longer timeframe by signed agreement between the VR Counselor and client. In addition, management reports and coaching tools have been enhanced to support supervisory oversight and monitoring of compliance with eligibility timelines and required procedures.

This finding demonstrates that further action is needed to ensure that service delivery practices fully comply with federal requirements as well as departmental policies and procedures for the development of an IPE. Corrective actions will be implemented to achieve more intensive supervisory review and follow-up to monitor development of IPEs within required timeframes, including adherence to required procedures when the timeframe must be extended.

The Department would like to note the "Description of Condition" and "Recommendations" sections do not completely align.

- *The Description of Condition specifically describes lack of compliance related to requirements and timelines for developing an IPE within 90-days.*
- *The recommendations are worded more broadly to reflect overall completion of the IPE.*

The Department's corrective action will specifically include items that assure compliance with required timeframes for development of IPEs.

Auditor's Concluding Remarks

We thank the Department for its cooperation and assistance throughout the audit. We will review the status of the Department's corrective action during our next audit.

Applicable Laws and Regulations

Title 2 U.S. Code of Federal Regulations Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance) establishes the following applicable requirements:

Section 200.303 Internal controls, states in part:

The non-Federal entity must:

- (a) Establish and maintain effective internal control over the Federal award that provides reasonable assurance that the non-Federal entity is managing the Federal award in compliance with Federal statutes, regulations, and the terms and conditions of the Federal award. These internal controls should be in compliance with guidance in "Standards for Internal Control in the Federal Government" issued by the Comptroller General of the United States or the "Internal Control Integrated Framework", issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).

- (b) Comply with Federal statutes, regulations, and the terms and conditions of the Federal awards.
- (d) Take prompt action when instances of noncompliance are identified including noncompliance identified in audit findings.

Section 200.516 Audit findings, states in part:

- (a) *Audit findings reported.* The auditor must report the following as audit findings in a schedule of findings and questioned costs:
 - (1) Significant deficiencies and material weaknesses in internal control over major programs and significant instances of abuse relating to major programs. The auditor's determination of whether a deficiency in internal control is a significant deficiency or material weakness for the purpose of reporting an audit finding is in relation to a type of compliance requirement for a major program identified in the Compliance Supplement.
 - (2) Material noncompliance with the provisions of Federal statutes, regulations, or the terms and conditions of Federal awards related to a major program. The auditor's determination of whether a noncompliance with the provisions of Federal statutes, regulations, or the terms and conditions of Federal awards is material for the purpose of reporting an audit finding is in relation to a type of compliance requirement for a major program identified in the compliance supplement.

The American Institute of Certified Public Accountants defines significant deficiencies and material weaknesses in internal controls over compliance in its *Codification of Statements on Auditing Standards*, section 935, Compliance Audits, as follows:

.11 For purposes of adapting GAAS to a compliance audit, the following terms have the meanings attributed as follows: ...

Deficiency in internal control over compliance. A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance on a timely basis. A deficiency in design exists when (a) a control necessary to meet the control objective is missing, or (b) an existing control is not properly designed so that, even if the control operates as designed, the control objective would not be met. A deficiency in operation exists when a properly designed control does not operate as designed or the person performing the control does not possess the necessary authority or competence to perform the control effectively.

Material weakness in internal control over compliance. A deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a compliance requirement will not be prevented, or detected and corrected, on a timely basis. In this section, a reasonable possibility exists when the likelihood of an event occurring is either reasonably possible or probable as defined as follows:

Reasonably possible. The chance of the future event or events occurring is more than remote but less than likely.

Probable. The future event or events are likely to occur.

Significant deficiency in internal control over compliance. A deficiency, or a combination of deficiencies, in internal control over compliance that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

Material noncompliance. In the absence of a definition of material noncompliance in the governmental audit requirement, a failure to follow compliance requirements or a violation of prohibitions included in the applicable compliance requirements that results in noncompliance that is quantitatively or qualitatively material, either individually or when aggregated with other noncompliance, to the affected government program.

29 U.S. Code 722 (b) Development of an individual plan for employment, states in part:

(3) Mandatory Procedures

(F) Timeframe for completing the individualized plan for employment

The individualized plan for employment shall be developed as soon as possible, but not later than a deadline of 90 days after the date of the determination of eligibility described in paragraph (1), unless the designated State unit and the eligible individual agree to an extension of that deadline to a specific date by which the individualized plan for employment shall be completed.

2018-023

The Department of Social and Health Services did not have adequate internal controls over and was not compliant with federal requirements to ensure payments paid on behalf of clients for Vocational Rehabilitation were allowable.

Federal Awarding Agency: Department of Education
Pass-Through Entity: None
CFDA Number and Title: 84.126 Rehabilitation Services – Vocational Rehabilitation Grants to States
Federal Award Number: H126A160071, H126A170071, H126A180071
Applicable Compliance Component: Activities Allowed or Unallowed and Allowable Costs/Cost Principles
Known Questioned Cost Amount: \$10,553

Background

The Department of Social and Health Services' Division of Vocational Rehabilitation (DVR) provides employment services and counseling to individuals with disabilities who want to work but experience barriers to work because of a physical, sensory, and/or mental disability. A DVR counselor works with each person to develop a customized plan of services designed to help them reach their employment goal. These services are primarily funded by the Vocational Rehabilitation Grant.

The Department operates and administers the program in accordance with federal laws and regulations, as well as with a State Plan that is approved every fiscal year. The Department spends federal grant money for employment services that are included in a client's individual plan for employment (IPE). The IPE helps a person with a disability in preparing for, securing, retaining or regaining an employment outcome. To ensure that the client is informed and involved in their employment outcome, both the client and a counselor must sign and date the completed IPE after reviewing it. Most services are not considered allowable unless they are in an approved IPE.

The Department may also spend federal grant money for pre-employment services that allow the Department to determine eligibility or ability to work and are not required to be in the IPE. While these expenses are not contained in an IPE, they still must be approved and have proper support.

The Department spent over \$55 million in federal program funds in fiscal year 2018, with about \$28 million paid for client services.

In prior audits, we reported that the Department did not have adequate internal controls over and was not compliant with requirements to ensure payments paid on behalf of clients were allowable. The prior finding numbers were 2017-014 and 2016-013.

Description of Condition

We found the Department did not establish adequate internal controls to ensure payments for client employment services were in an approved IPE. We used a statistical sampling method to randomly select and examine 63 of the 35,704 total payments over \$50 made for client services during fiscal year 2018. We examined each payment to determine if it was an allowable employment service included in a client's IPE or a pre-employment service.

In 13 cases (21 percent), we found payments totaling \$20,287 were improper, \$10,553 of which was paid with federal funds. Specifically:

- In four cases, the IPE was not signed by client
- In six cases, the service provided was not in the IPE
- In four cases, the Department could not provide an IPE

We also examined these 63 payments to verify the authorization for payment was made after the IPE had been approved. We found three payments (5 percent) when the authorization was made before an approved IPE was completed.

We consider these internal control deficiencies to be a material weakness.

Cause of Condition

Department staff did not follow established policies and procedures to ensure that payments for client services were contained in the client's approved IPE and services were not being paid for before approval. Managerial oversight was not sufficient to detect or prevent these issues.

Effect of Condition and Questioned Costs

By not having adequate internal controls in place, the Department increases its risk of making improper payments for client services.

A statistical sampling method was used to randomly select the payments examined in the audit. Based on the results of our testing, we estimate the total amount of likely improper payments with federal funds to be \$2,965,496. Many of the improper payments were funded by state dollars. We found \$9,734 of improper state payments, which projects to a likely improper payment amount of \$3,580,400. This amount is not included in the federal questioned costs.

Our sampling methodology meets statistical sampling criteria under generally accepted auditing standards in AU-C 530.05. It is important to note that the sampling technique we used is intended to support our audit conclusions by determining if expenditures complied with program requirements in all material respects. Accordingly, we used an acceptance sampling formula designed to provide a high level of assurance, with a 95 percent confidence of whether exceptions exceeded our materiality threshold. Our audit report and finding reflects this conclusion. However, the likely improper payment projections are a point estimate and only represent our "best estimate of total questioned costs" as required by 2 CFR 200.516(3). To ensure a representative sample, we stratified the population by dollar amount.

We question costs when we find an agency has not complied with grant regulations or when it does not have adequate documentation to support its expenditures.

Recommendations

We recommend the Department:

- Pay for client employment services only when those services are contained in an approved IPE
- Ensure services are not paid for before being properly approved
- Ensure managers adequately monitor staff to ensure federal requirements are met

Department's Response

The Department concurs with the finding.

The Department has implemented additional procedural guidance and enhanced management reports aimed at ensuring full compliance with federal requirements that certain client services must be contained in an approved IPE prior to delivery. In addition, management reports and coaching tools have been enhanced to support supervisory oversight and monitoring of compliance with IPE requirements.

This finding demonstrates that further action is needed to ensure that service delivery practices fully comply with federal requirements as well as departmental policies and procedures.

Corrective actions will be implemented to achieve more intensive supervisory review and follow-up to monitor client service expenditures and assure compliance with IPE requirements.

Auditor's Concluding Remarks

We thank the Department for its cooperation and assistance throughout the audit. We will review the status of the Department's corrective action during our next audit.

Applicable Laws and Regulations

Title 2 U.S. Code of Federal Regulations Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance) establishes the following applicable requirements:

Section 200.53 Improper Payments states:

- (a) *Improper payment* means any payment that should not have been made or that was made in an incorrect amount (including overpayments and underpayments) under statutory, contractual, administrative, or other legally applicable requirements; and
- (b) *Improper payment* includes any payment to an ineligible party, any payment for an ineligible good or service, any duplicate payment, any payment for a good or service not received (except for such payments where authorized by law), any payment that does not account for credit for applicable discounts, and any payment where insufficient or

lack of documentation prevents a reviewer from discerning whether a payment was proper.

Section 200.303 Internal controls, states in part:

The non-Federal entity must:

- (a) Establish and maintain effective internal control over the Federal award that provides reasonable assurance that the non-Federal entity is managing the Federal award in compliance with Federal statutes, regulations, and the terms and conditions of the Federal award. These internal controls should be in compliance with guidance in “Standards for Internal Control in the Federal Government” issued by the Comptroller General of the United States or the “Internal Control Integrated Framework”, issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).
- (b) Comply with Federal statutes, regulations, and the terms and conditions of the Federal awards.
- (d) Take prompt action when instances of noncompliance are identified including noncompliance identified in audit findings.

Section 200.403 Factors affecting Allowability of costs.

Except where otherwise authorized by statute, costs must meet the following general criteria in order to be allowable under Federal awards.

- (a) Be necessary and reasonable for the performance of the Federal award and be allocable thereto under these principles.
- (b) Conform to any limitations or exclusions set forth in these principles or in the Federal award as to types or amount of cost items.
- (c) Be consistent with policies and procedures that apply uniformly to both federally-financed and other activities of the non-Federal entity.
- (d) Be accorded consistent treatment. A cost may not be assigned to a Federal award as a direct cost if any other cost incurred for the same purpose in like circumstances has been allocated to the Federal award as an indirect cost.
- (e) Be determined in accordance with generally accepted accounting principles (GAAP), except, for state and local governments and Indian tribes only, as otherwise provided for in this part.
- (f) Not be included as a cost or used to meet cost sharing or matching requirements of any other federally-financed program in either the current or a prior period. See also §200.306 Cost sharing or matching paragraph (b).
- (g) Be adequately documented. See also §§200.300 Statutory and national policy requirements through 200.309 Period of performance of this part.

Section 200.410 Collection of unallowable costs.

Payments made for costs determined to be unallowable by either the Federal awarding agency, cognizant agency for indirect costs, or pass-through entity, either as direct or indirect costs, must be refunded (including interest) to the Federal Government in accordance with instructions from the Federal agency that determined the costs are unallowable unless Federal statute or regulation directs otherwise. See also Subpart D— Post Federal Award Requirements of this part, §§200.300 Statutory and national policy requirements through 200.309 Period of performance.

Section 200.516 Audit findings, states in part:

- (a) *Audit findings reported.* The auditor must report the following as audit findings in a schedule of findings and questioned costs:
- (1) Significant deficiencies and material weaknesses in internal control over major programs and significant instances of abuse relating to major programs. The auditor's determination of whether a deficiency in internal control is a significant deficiency or material weakness for the purpose of reporting an audit finding is in relation to a type of compliance requirement for a major program identified in the Compliance Supplement.
 - (2) Material noncompliance with the provisions of Federal statutes, regulations, or the terms and conditions of Federal awards related to a major program. The auditor's determination of whether a noncompliance with the provisions of Federal statutes, regulations, or the terms and conditions of Federal awards is material for the purpose of reporting an audit finding is in relation to a type of compliance requirement for a major program identified in the compliance supplement.
 - (3) Known questioned costs that are greater than \$25,000 for a type of compliance requirement for a major program. Known questioned costs are those specifically identified by the auditor. In evaluating the effect of questioned costs on the opinion on compliance, the auditor considers the best estimate of total costs questioned (likely questioned costs), not just the questioned costs specifically identified (known questioned costs). The auditor must also report known questioned costs when likely questioned costs are greater than \$25,000 for a type of compliance requirement for a major program. In reporting questioned costs, the auditor must include information to provide proper perspective for judging the prevalence and consequences of the questioned costs.

The American Institute of Certified Public Accountants defines significant deficiencies and material weaknesses in internal controls over compliance in its *Codification of Statements on Auditing Standards*, section 935, Compliance Audits, as follows:

.11 For purposes of adapting GAAS to a compliance audit, the following terms have the meanings attributed as follows: ...

Deficiency in internal control over compliance. A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance on a timely basis. A deficiency in design exists when (a) a control necessary to meet the control objective is missing, or (b) an existing control is not properly designed so that, even if the control operates as designed, the control objective would not be met. A deficiency in operation exists when a properly designed control does not operate as designed or the person performing the control does not possess the necessary authority or competence to perform the control effectively.

Material weakness in internal control over compliance. A deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a compliance requirement will not be prevented, or detected and corrected, on a timely basis. In this section, a reasonable possibility exists when

the likelihood of an event occurring is either reasonably possible or probable as defined as follows:

Reasonably possible. The chance of the future event or events occurring is more than remote but less than likely.

Probable. The future event or events are likely to occur.

Significant deficiency in internal control over compliance. A deficiency, or a combination of deficiencies, in internal control over compliance that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

Material noncompliance. In the absence of a definition of material noncompliance in the governmental audit requirement, a failure to follow compliance requirements or a violation of prohibitions included in the applicable compliance requirements that results in noncompliance that is quantitatively or qualitatively material, either individually or when aggregated with other noncompliance, to the affected government program.

29 U. S. Code. section 722. Eligibility and individual plan for employment, states in part:

(a) Eligibility

(2) Presumption of benefit

(A) Applicants

For purposes of this section, an individual shall be presumed to be an individual that can benefit in terms of an employment outcome from vocational rehabilitation services under section 705(20)(A) of this title.

(B) Responsibilities

Prior to determining under this subsection that an applicant described in subparagraph (A) is unable to benefit due to the severity of the individual's disability or that the individual is ineligible for vocational rehabilitation services, the designated State unit shall explore the individual's abilities, capabilities, and capacity to perform in work situations, through the use of trial work experiences, as described in section 705(2)(D) of this title, with appropriate supports provided through the designated State unit. Such experiences shall be of sufficient variety and over a sufficient period of time to determine the eligibility of the individual. In providing the trial experiences, the designated State unit shall provide the individual with the opportunity to try different employment experiences, including supported employment, and the opportunity to become employed in competitive integrated employment.

(b) Development of an individual plan for employment

(3) Mandatory procedures

(C) Signatories

An individualized plan for employment shall be—

(i) agreed to, and signed by, such eligible individual or, as appropriate, the individual's representative; and

(ii) approved and signed by a qualified vocational rehabilitation counselor employed by the designated State unit.

2018-024

The Department of Social and Health Services did not have adequate internal controls to ensure its federal financial reports for the Vocational Rehabilitation grant were accurately prepared.

Federal Awarding Agency: U.S. Department of Education
Pass-Through Entity: None
CFDA Number and Title: 84.126 Rehabilitation Services – Vocational Rehabilitation Grants to States
Federal Award Number: H126A160071, H126A170071, H126A180071
Applicable Compliance Component: Reporting
Known Questioned Cost Amount: None

Background

The Department of Social and Health Services' (Department) Division of Vocational Rehabilitation provides employment services and counseling to individuals with disabilities who want to work but experience barriers to work because of a physical, sensory and/or mental disability. A Department counselor works with each person to develop a customized plan of services designed to help them reach their employment goal. These services are primarily funded by the Vocational Rehabilitation grant.

The Department must submit a program cost report (RSA-2), which is used to report expenditures for particular services, numbers of clients served, numbers of staff, and amounts transferred in and out of the program. The grantor uses this information to evaluate and monitor the financial performance and achievements of a state's vocational rehabilitation agency. The report must be completed annually and is due by December 31 after the close of the federal fiscal year and must include information about all open grant awards.

The Department also must submit a Federal Financial Report SF-425, which is used to report expenditures for federal grants semiannually. The report requires disclosure of cash receipts, disbursements, and cash on hand for the grant during the reporting period. Additional information on the report includes disclosure of the indirect costs, program costs, and signature of a certifying individual.

Description of Condition

We found the Department did not have adequate internal controls to ensure its federal financial reports for the Vocational Rehabilitation grant were accurately prepared.

Processes, such as a secondary review, were not in place that would detect errors in the RSA-2 or SF-425 reports before the Department submitted them to the federal grantor.

We consider this internal control deficiency to be a material weakness. This condition was not reported in the prior audit.

Cause of Condition

In the prior audit, we confirmed the Department had a secondary review of these reports in place. The person who performed the reviews left the Department, and management did not ensure a secondary review process continued.

Effect of Condition

By not establishing adequate internal controls, the Department increases the risk that it could misreport information to the grantor.

Recommendation

We recommend the Department improve its internal controls by re-implementing a secondary review of the RSA-2 and SF-425 reports.

Department's Response

The Department concurs with the finding.

The Department has established written procedures to re-implement secondary reviews for the reports.

Secondary reviews have been completed for the most recent SF-425 report that was submitted in September 2018 and secondary reviews of future RSA-2 and SF-425 reports will occur.

Auditor's Concluding Remarks

We thank the Department for its cooperation and assistance throughout the audit. We will review the status of the Department's corrective action during our next audit.

Applicable Laws and Regulations

Title 2 U.S. Code of Federal Regulations Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance) establishes the following applicable requirements:

Section 200.303 Internal controls, states in part:

The non-Federal entity must:

- (a) Establish and maintain effective internal control over the Federal award that provides reasonable assurance that the non-Federal entity is managing the Federal award in compliance with Federal statutes, regulations, and the terms and conditions of the Federal award. These internal controls should be in compliance with guidance in "Standards for Internal Control in the Federal Government" issued by the Comptroller General of the United States or the "Internal Control Integrated Framework", issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).

Section 200.516 Audit findings, states in part:

(a) *Audit findings reported.* The auditor must report the following as audit findings in a schedule of findings and questioned costs:

(1) Significant deficiencies and material weaknesses in internal control over major programs and significant instances of abuse relating to major programs. The auditor's determination of whether a deficiency in internal control is a significant deficiency or material weakness for the purpose of reporting an audit finding is in relation to a type of compliance requirement for a major program identified in the Compliance Supplement.

The American Institute of Certified Public Accountants defines significant deficiencies and material weaknesses in internal controls over compliance in its *Codification of Statements on Auditing Standards*, section 935, Compliance Audits, as follows:

.11 For purposes of adapting GAAS to a compliance audit, the following terms have the meanings attributed as follows: ...

Deficiency in internal control over compliance. A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance on a timely basis. A deficiency in design exists when (a) a control necessary to meet the control objective is missing, or (b) an existing control is not properly designed so that, even if the control operates as designed, the control objective would not be met. A deficiency in operation exists when a properly designed control does not operate as designed or the person performing the control does not possess the necessary authority or competence to perform the control effectively.

Material weakness in internal control over compliance. A deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a compliance requirement will not be prevented, or detected and corrected, on a timely basis. In this section, a reasonable possibility exists when the likelihood of an event occurring is either reasonably possible or probable as defined as follows:

Reasonably possible. The chance of the future event or events occurring is more than remote but less than likely.

Probable. The future event or events are likely to occur.

Significant deficiency in internal control over compliance. A deficiency, or a combination of deficiencies, in internal control over compliance that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

2018-025

The Department of Social and Health Services did not have adequate internal controls over and did not comply with federal requirements to ensure subrecipients of the Substance Abuse and Mental Health Services Projects of Regional and National Significance and Block Grants for Prevention and Treatment of Substance Abuse programs received required audits.

Federal Awarding Agency: U.S. Department of Health and Human Services
Pass-Through Entity: None
CFDA Number and Title: 93.243 Substance Abuse and Mental Health Services
Projects of Regional and National
Significance
93.959 Block Grants for Prevention and Treatment of
Substance Abuse
Federal Award Number: 2B08TI010056-16; 2B08TI010056-17; 5U79TI023477-
05; 5U79SP020155-03; 5U79TI024265-03;
1H79TI025995-01; 5H79SM061705-02;
5H79TI025342-02; 1H79TI026138-01; 1H79TI025570-
01; 1H79SP022135-01
Applicable Compliance Component: Subrecipient Monitoring
Known Questioned Cost Amount: None

Background

The Department of Social and Health Services (Department), Behavioral Health Administration (BHA), administers the Block Grants for Prevention and Treatment of Substance Abuse. The Department subawards some of the funds to counties, tribes, nonprofit organizations and other state agencies to develop prevention programs and provide treatment and support services. The Department spent more than \$32.8 million in grant funds during fiscal year 2018. Of this amount, the Department passed about \$11 million to 76 subrecipients.

The Department also administers the Substance Abuse and Mental Health Services Projects of Regional and National Significance. This program addresses priority substance abuse treatment, prevention and mental health needs of regional and national significance. The Department spent more than \$8 million in grant funds during fiscal year 2018 and passed about \$1.8 million of this amount to 39 subrecipients, including counties, school districts and nonprofit organizations.

Federal regulations require the Department to monitor the activities of its subrecipients. This includes verifying that its subrecipients that spend \$750,000 or more in federal awards during a fiscal year obtain a single audit. Further, for the awards it passes on to its subrecipients, the Department must follow up and ensure its subrecipients take timely action on all deficiencies detected through audits, onsite reviews and other means, and must issue a management decision for audit findings within six months of the audit report's acceptance by the Federal Audit Clearinghouse. These requirements help ensure grant money is used for authorized purposes and within the provisions of contracts or grant agreements.

As of July 1, 2018, the operations management of the BHA was transferred from the Department to the Health Care Authority (Authority). The Authority assumed the responsibilities over the Block Grants for Prevention and Treatment of Substance Abuse and Substance Abuse and Mental Health Services Projects of Regional and National Significance.

In prior audits, we reported the Department did not have internal controls over and did not comply with requirements to ensure subrecipients received required audits. The prior finding numbers were 2017-016, 2016-014, 2015-016 and 2014-019.

Description of Condition

BHA did not have adequate internal controls over and did not comply with federal requirements to ensure subrecipients of the Substance Abuse and Mental Health Services Projects of Regional and National Significance and Block Grants for Prevention and Treatment of Substance Abuse programs received required audits.

We found BHA did not have adequate internal controls in place to verify:

- Subrecipients received required audits
- Findings were followed up on and management decisions were issued when due

BHA implemented a new process to obtain and monitor information related to required subrecipient audits beginning in April 2016. As part of this process, BHA sends audit verification forms to all subrecipients and contractors that receive federal funds, asking whether they required an audit and, if so, to provide a copy of the audit report. When the forms are returned, the results are to be tracked and monitored in a tracking spreadsheet.

We evaluated BHA's process and found 47 subrecipients of the Block Grants for Prevention and Treatment of Substance Abuse and all 39 subrecipients of the Substance Abuse and Mental Health Services Projects of Regional and National Significance programs were not monitored to ensure their compliance with requirements for single audits of subrecipients.

We consider these internal control weaknesses to constitute a material weakness.

Cause of Condition

While BHA had established procedures to monitor and verify if subrecipients obtained required audits, it did not follow them. Specifically, when the staff member assigned to perform the audit tracking duties left BHA in July 2017, management did not ensure other BHA staff performed those responsibilities.

Effect of Condition

Without establishing adequate internal controls, BHA cannot ensure all subrecipients that met the threshold for an audit complied with federal grant requirements. In addition, one subrecipient received an audit finding that BHA did not perform follow up on, as required.

Recommendations

Since the Authority now manages these grant funds, we recommend management:

- Ensure that established procedures related to subrecipient audit monitoring are followed
- Verify all required audits occurred
- Follow up on subrecipient audit findings related to the program and issue a management decision promptly

Department's Response

The Department concurs with the finding.

Audit verification forms are sent to contractors and they are asked to declare if they receive \$750,000 or more in federal funds. If they do, they are asked to send in a copy of the required single audit.

For a majority of the contractors such as counties, tribal nations and school districts; a single audit is required and performed every year. These audits can be found in the Federal Audit Clearinghouse database. While these audits were not tracked by staff in a spreadsheet, a majority of the audits were found in the Department's contracting database.

Of the 47 Subrecipients of the Block Grants for Prevention and Treatment of Substance Abuse and the 39 Subrecipients of the Substance Abuse and Mental Health Services Projects of Regional and National Significance programs, staff found the following in the Department's contracting database:

- 42 of the 47 audits.
- 34 of the 39 audits.

While 76 of the 86 audits were found, the Department's contracting database does not include a date of when these audits were downloaded for record-keeping and they were not tracked as per procedures.

Currently, single audits for counties and tribal nations are now tracked on a spreadsheet. This spreadsheet contains single audits going back to FY15.

The Authority will ensure:

- *Established procedures related to subrecipient audit monitoring are followed.*
- *Required audits occur.*
- *Subrecipient audit findings, related to the program, are followed up on.*

Auditor's Concluding Remarks

We thank the Department for its cooperation and assistance throughout the audit. We will review the status of the Department's corrective action during our next audit.

Applicable Laws and Regulations

Title 2 U.S. Code of Federal Regulations Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance) establishes the following applicable requirements:

Section 200.303 Internal controls, states in part:

The non-Federal entity must:

- (a) Establish and maintain effective internal control over the Federal award that provides reasonable assurance that the non-Federal entity is managing the Federal award in compliance with Federal statutes, regulations, and the terms and conditions of the Federal award. These internal controls should be in compliance with guidance in "Standards for Internal Control in the Federal Government" issued by the Comptroller General of the United States or the "Internal Control Integrated Framework", issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).
- (b) Comply with Federal statutes, regulations, and the terms and conditions of the Federal awards.
- (d) Take prompt action when instances of noncompliance are identified including noncompliance identified in audit findings.

Section 200.516 Audit findings, states in part:

- (a) *Audit findings reported.* The auditor must report the following as audit findings in a schedule of findings and questioned costs:
 - (1) Significant deficiencies and material weaknesses in internal control over major programs and significant instances of abuse relating to major programs. The auditor's determination of whether a deficiency in internal control is a significant deficiency or material weakness for the purpose of reporting an audit finding is in relation to a type of compliance requirement for a major program identified in the Compliance Supplement.
 - (2) Material noncompliance with the provisions of Federal statutes, regulations, or the terms and conditions of Federal awards related to a major program. The auditor's determination of whether a noncompliance with the provisions of Federal statutes, regulations, or the terms and conditions of Federal awards is material for the purpose of reporting an audit finding is in relation to a type of compliance requirement for a major program identified in the compliance supplement.

Section 200.331 Requirements for pass-through entities, states in part:

All pass-through entities must:

- (d) Monitor the activities of the subrecipient as necessary to ensure that the subaward is used for authorized purposes, in compliance with Federal statutes, regulations, and the

terms and conditions of the subaward; and that subaward performance goals are achieved. Pass-through entity monitoring of the subrecipient must include:

- (1) Reviewing financial and performance reports required by the pass-through entity.
- (2) Following-up and ensuring that the subrecipient takes timely and appropriate action on all deficiencies pertaining to the Federal award provided to the subrecipient from the pass-through entity detected through audits, on-site reviews, and other means.
- (3) Issuing a management decision for audit findings pertaining to the Federal award provided to the subrecipient from the pass-through entity as required by §200.521 Management decision.
 - (f) Verify that every subrecipient is audited as required by Subpart F—Audit Requirements of this part when it is expected that the subrecipient's Federal awards expended during the respective fiscal year equaled or exceeded the threshold set forth in §200.501 Audit requirements.

The American Institute of Certified Public Accountants defines significant deficiencies and material weaknesses in internal controls over compliance in its *Codification of Statements on Auditing Standards*, section 935, Compliance Audits, as follows:

.11 For purposes of adapting GAAS to a compliance audit, the following terms have the meanings attributed as follows: ...

Deficiency in internal control over compliance. A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance on a timely basis. A deficiency in design exists when (a) a control necessary to meet the control objective is missing, or (b) an existing control is not properly designed so that, even if the control operates as designed, the control objective would not be met. A deficiency in operation exists when a properly designed control does not operate as designed or the person performing the control does not possess the necessary authority or competence to perform the control effectively.

Material weakness in internal control over compliance. A deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a compliance requirement will not be prevented, or detected and corrected, on a timely basis. In this section, a reasonable possibility exists when the likelihood of an event occurring is either reasonably possible or probable as defined as follows:

Reasonably possible. The chance of the future event or events occurring is more than remote but less than likely.

Probable. The future event or events are likely to occur.

Significant deficiency in internal control over compliance. A deficiency, or a combination of deficiencies, in internal control over compliance that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

Material noncompliance. In the absence of a definition of material noncompliance in the governmental audit requirement, a failure to follow compliance requirements or a violation of prohibitions included in the applicable compliance requirements that results in noncompliance that is quantitatively or qualitatively material, either individually or when aggregated with other noncompliance, to the affected government program.

2018-026 **The Department of Social and Health Services did not have adequate internal controls over and was not compliant with requirements to ensure payments to child care providers paid with Temporary Assistance for Needy Families funds were allowable.**

Federal Awarding Agency: U.S. Department of Health and Human Services
Pass-Through Entity: None
CFDA Number and Title: 93.558 Temporary Assistance for Needy Families
Federal Award Number: 1801WATANF; 1801WATAN3; 1701WATANF; 1701WATAN3
Applicable Compliance Component: Activities Allowed or Unallowed and Allowable Costs/Cost Principles
Known Questioned Cost Amount: \$2,252

Background

The Department of Social and Health Services (DSHS), Community Services Division, administers the Temporary Assistance for Needy Families (TANF) grant that provides temporary cash assistance for families in need. To receive TANF benefits, participants must be engaged in activities listed in the Individual Responsibility Plan (IRP) through the WorkFirst program, unless the TANF benefits are received only on behalf of a child. TANF funds may be used to pay participants' childcare costs to meet one of the program's primary purposes of helping clients obtain employment. If a client obtains employment and is no longer eligible for the program, TANF funds may still be used to pay childcare costs to help the client maintain employment.

Working Connections Child Care program

Washington has established the Working Connections Child Care (WCCC) program to help eligible working families pay for childcare. Both the Department of Children, Youth and Families (DCYF) (formerly the Department of Early Learning) and DSHS administer the program. DCYF is responsible for establishing policies and procedures for the program and for licensing childcare providers. DSHS determines client eligibility and pays childcare providers under an agreement with DCYF.

Federal grant funding

Some payments made to WCCC providers for childcare are paid for by both the Child Care and Development Fund (CCDF) grant and the TANF grant. While the two federal programs are separate, the requirements and policies in Washington for childcare payments are consolidated under the WCCC program.

In fiscal year 2018, DSHS made an estimated 639,816 monthly childcare subsidy payments to childcare providers from both the CCDF and TANF grant as well as state funding. These payments totaled almost \$267 million in federal funds, about \$77 million of which came from the TANF grant.

Childcare providers

The WCCC program includes three provider types:

- Licensed centers
- Licensed family homes
- Family, friends and neighbors (FFN)

According to state rules, childcare providers must maintain attendance records to support their billing. At a minimum, the records must include: the children's names; date(s) childcare was provided; and authorized signatures, typically of a parent or guardian, documenting the times the child arrived and left care.

Prior audit results

In the prior audit, we reported DSHS did not have adequate internal controls over and did not comply with federal requirements to ensure payments to childcare providers, paid for by TANF funds, were allowable. The prior audit finding number was 2017-017 and 2016-019. We have also been reporting on the same condition for the CCDF program since 2005. The most recent audit finding numbers were 2017-024, 2016-021, 2015-023, 2014-023, 2013-016, 12-28, 11-23, 10-31, 9-12 and 8-13.

Description of Condition

We found that the internal control deficiencies identified during our audit of the CCDF program directly affect DSHS use of TANF funds, because the federal grants are commingled when paying WCCC providers.

We found DSHS did not have adequate internal controls to ensure payments to childcare providers, paid for by TANF funds, were allowable. Although DCYF and DSHS perform some oversight activities, these were not sufficient to ensure payments were allowable.

We used a statistical sampling method to randomly select and examine 133 payments for child care to determine if they were allowable. We chose child care payments by totals from each of the three provider types: licensed centers, licensed family homes and FFN's. With assistance from DCYF, we requested attendance records from providers that supported the payments. We reviewed each provider's records to determine if the payments were allowed by federal and state regulations, as well as by DCYF's policies.

We found 22 (16 percent) payments with TANF federal funding were partially or fully unallowable. All of these payments were partially paid for by TANF funds. In total, we questioned \$2,252 paid by federal TANF funds.

The overpayments occurred because:

- Providers did not submit attendance records in response to our request, or submitted records that were inadequate to support payments
- Providers overbilled for services not performed or not supported by attendance records
- Providers billed for overtime, field trip fees and registration fees when they did not have a written policy in place to also charge these same fees to private paying parents
- Providers were not paid the correct rate based on the child's age and region

We consider these internal control deficiencies to be a significant deficiency.

Cause of Condition

While DSHS authorizations to provide services establish a maximum for what providers may bill without further approval, it does not prevent providers from billing for unallowable days, hours or services. The claim and payment system is not linked to authorizations or attendance. Childcare providers must keep attendance records and submit this documentation only when it is requested.

DCYF management asserts the identified internal control weaknesses are unlikely to be resolved without an electronic time and attendance reporting system. DCYF has finalized the procurement of a system that will maintain electronic copies of attendance records and potentially reduce provider errors. This system began operating in October 2018 and is expected to enable DCYF to perform data analysis and audit of all payments. In addition, new rules and policies for providers have been written, but have not been implemented due to timing.

Effect of Condition and Questioned Costs

By not having adequate internal controls in place, DSHS increases its risk of making improper payments for childcare services.

A statistical sampling method was used to randomly select the payments examined in the audit. Based on the results of our testing, we estimate the total amount of likely improper payments with federal TANF funds to be \$10,765,887. Many of the improper payments were partially funded by state dollars. We found \$129 of improper state payments, which projects to a likely improper payment amount of \$617,246. This amount is not included in the federal questioned costs.

Our sampling methodology meets statistical sampling criteria under generally accepted auditing standards in AU-C 530.05. It is important to note that the sampling technique we used is intended to support our audit conclusions by determining if expenditures complied with program requirements in all material respects. Accordingly, we used an acceptance sampling formula designed to provide a very high level of assurance, with a 99 percent confidence of whether exceptions exceeded our materiality threshold. Our audit report and finding reflects this conclusion. However, the likely improper payment projections are a point estimate and only represent our "best estimate of total questioned costs" as required by 2 CFR 200.516(3). To ensure a representative sample, we stratified the population by dollar amount.

We question costs when we find an agency has not complied with grant regulations or when it does not have adequate documentation to support its expenditures.

Recommendations

We recommend the Department:

- Implement preventive internal controls over payments to providers to reduce the rate of unallowable payments
- Consult with the grantor to discuss whether the questioned costs identified in the audit should be repaid

Department's Response

The Department appreciates, acknowledges and supports the State Auditor's Office's (SAO) mission, which is to hold state and local governments accountable for the use of public resources.

The Department partially concurs with the overall findings of the SAO.

In response to DSHS 2017-017 TANF Activities Allowed Finding, the Department implemented internal controls including third-party reviews through the establishment of the Process Review Panel (PRP), and pre-authorization reviews on high-risk and/or high cost cases based on trend analysis discovered during the PRP. These initiatives help ensure staff make correct eligibility and authorization determinations which minimizes the risk for providers to overbill or incorrectly bill for payments.

The Department implemented most of these internal controls during the state fiscal year (SFY) 18 audit period, therefore, we acknowledged we were likely to see similar findings during this audit.

SAO Description of Weakness: *Providers overbilled for services not performed or supported by required documentation. Adequate internal controls did not exist to ensure payments were allowable. Although the authorizations establish a maximum for what providers may bill without further approval, they do not prevent providers from billing for unallowable days, hours or services.*

The Department acknowledges that adequate attendance records are necessary in the reconciliation process to determine allowable payments. The Department of Children, Youth, and Families (DCYF) policy requires providers receiving subsidy payments to maintain attendance records and provide them upon request. However, because attendance records are paper-based, it is not feasible for staff to request, review and reconcile all records before subsidy payments are made. As referenced in the report above, the Department collaborated with DCYF on procurement for an electronic attendance system.

Effective December 1, 2018, DCYF requires all licensed providers who accept subsidy to use DCYF's electronic attendance system or an approved third party system to track attendance. DCYF's system enables accurate, real-time recording of child care attendance, tracks daily attendance, and captures data on child care usage. FFN providers are required to use DCYF's system or an approved third party system for tracking attendance by November 30, 2019.

The Department will continue to conduct post-payment reviews, or refer to DCYF for review, where it appears likely that an improper payment may have occurred. Reviews include requesting attendance records to determine whether an overpayment occurred, whether it was a provider or a client that was overpaid, the amount of the improper payment and establishing an overpayment if appropriate.

Beginning July 1, 2019, the Department will transfer responsibility for administering all aspects of client eligibility determination and child care provider payment under the Child Care Development Fund (CCDF) to DCYF. While the Department continues to play an active role in supporting continuous improvements within the Working Connections Child Care Program, we acknowledge that subsequent changes and enhancements to this program are within the purview of DCYF.

If the grantor contacts the Department regarding questioned costs that should be repaid, the Department will confirm these costs with HHS and will take appropriate action.

Auditor's Concluding Remarks

We thank the Department for its cooperation and assistance throughout the audit. We will review the status of the Department's corrective action during our next audit.

Applicable Laws and Regulations

Title 2 U.S. Code of Federal Regulations Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance) establishes the following applicable requirements:

Section 200.53 Improper Payments states:

- (a) *Improper payment* means any payment that should not have been made or that was made in an incorrect amount (including overpayments and underpayments) under statutory, contractual, administrative, or other legally applicable requirements; and
- (b) *Improper payment* includes any payment to an ineligible party, any payment for an ineligible good or service, any duplicate payment, any payment for a good or service not received (except for such payments where authorized by law), any payment that does not account for credit for applicable discounts, and any payment where insufficient or lack of documentation prevents a reviewer from discerning whether a payment was proper.

Section 200.303 Internal controls, states in part:

The non-Federal entity must:

- (a) Establish and maintain effective internal control over the Federal award that provides reasonable assurance that the non-Federal entity is managing the Federal award in compliance with Federal statutes, regulations, and the terms and conditions of the Federal award. These internal controls should be in compliance with guidance in "Standards for Internal Control in the Federal Government" issued by the Comptroller

General of the United States or the “Internal Control Integrated Framework”, issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). (d)

Take prompt action when instances of noncompliance are identified including noncompliance identified in audit findings.

Section 200.403 Factors affecting Allowability of costs.

Except where otherwise authorized by statute, costs must meet the following general criteria in order to be allowable under Federal awards.

- (a) Be necessary and reasonable for the performance of the Federal award and be allocable thereto under these principles.
- (b) Conform to any limitations or exclusions set forth in these principles or in the Federal award as to types or amount of cost items.
- (c) Be consistent with policies and procedures that apply uniformly to both federally-financed and other activities of the non-Federal entity.
- (d) Be accorded consistent treatment. A cost may not be assigned to a Federal award as a direct cost if any other cost incurred for the same purpose in like circumstances has been allocated to the Federal award as an indirect cost.
- (e) Be determined in accordance with generally accepted accounting principles (GAAP), except, for state and local governments and Indian tribes only, as otherwise provided for in this part.
- (f) Not be included as a cost or used to meet cost sharing or matching requirements of any other federally-financed program in either the current or a prior period. See also §200.306 Cost sharing or matching paragraph (b).
- (g) Be adequately documented. See also §§200.300 Statutory and national policy requirements through 200.309 Period of performance of this part.

Section 200.410 Collection of unallowable costs.

Payments made for costs determined to be unallowable by either the Federal awarding agency, cognizant agency for indirect costs, or pass-through entity, either as direct or indirect costs, must be refunded (including interest) to the Federal Government in accordance with instructions from the Federal agency that determined the costs are unallowable unless Federal statute or regulation directs otherwise. See also Subpart D—Post Federal Award Requirements of this part, §§200.300 Statutory and national policy requirements through 200.309 Period of performance.

Section 200.516 Audit findings, states in part:

- (a) *Audit findings reported.* The auditor must report the following as audit findings in a schedule of findings and questioned costs:
 - (1) Significant deficiencies and material weaknesses in internal control over major programs and significant instances of abuse relating to major programs. The auditor’s determination of whether a deficiency in internal control is a significant

deficiency or material weakness for the purpose of reporting an audit finding is in relation to a type of compliance requirement for a major program identified in the Compliance Supplement.

- (3) Known questioned costs that are greater than \$25,000 for a type of compliance requirement for a major program. Known questioned costs are those specifically identified by the auditor. In evaluating the effect of questioned costs on the opinion on compliance, the auditor considers the best estimate of total costs questioned (likely questioned costs), not just the questioned costs specifically identified (known questioned costs). The auditor must also report known questioned costs when likely questioned costs are greater than \$25,000 for a type of compliance requirement for a major program. In reporting questioned costs, the auditor must include information to provide proper perspective for judging the prevalence and consequences of the questioned costs.

The American Institute of Certified Public Accountants defines significant deficiencies and material weaknesses in internal controls over compliance in its *Codification of Statements on Auditing Standards*, section 935, Compliance Audits, as follows:

- .11 For purposes of adapting GAAS to a compliance audit, the following terms have the meanings attributed as follows: ...

Deficiency in internal control over compliance. A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance on a timely basis. A deficiency in design exists when (a) a control necessary to meet the control objective is missing, or (b) an existing control is not properly designed so that, even if the control operates as designed, the control objective would not be met. A deficiency in operation exists when a properly designed control does not operate as designed or the person performing the control does not possess the necessary authority or competence to perform the control effectively.

Material weakness in internal control over compliance. A deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a compliance requirement will not be prevented, or detected and corrected, on a timely basis. In this section, a reasonable possibility exists when the likelihood of an event occurring is either reasonably possible or probable as defined as follows:

Reasonably possible. The chance of the future event or events occurring is more than remote but less than likely.

Probable. The future event or events are likely to occur.

Significant deficiency in internal control over compliance. A deficiency, or a combination of deficiencies, in internal control over compliance that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

45 CFR Subpart A, 260.20, What is the purpose of the TANF program? States:

The TANF program has the following four purposes

- (a) Provide assistance to needy families so that children may be cared for in their own homes or in the homes of relatives;
- (b) End the dependence of needy parents on government benefits by promoting job preparation, work, and marriage;
- (c) Prevent and reduce the incidence of out-of-wedlock pregnancies and establish annual numerical goals for preventing and reducing the incidence of these pregnancies; and
- (d) Encourage the formation and maintenance of two-parent families.

WAC 170-290-0002 Scope of agency responsibilities.

DEL is designated as the lead agency for child care and development funds (CCDF) and oversees expenditure of CCDF funds.

- (1) The responsibilities of the department of early learning (DEL) include, but are not limited to:
 - (a) Determining child care subsidy policy for the WCCC and SCC programs;
 - (b) Determining thresholds for eligibility and copayment amounts and establishing rights and responsibilities; and
 - (c) Serving as the designated representative for the state to implement the collective bargaining agreement under RCW 41.56.028 for in-home/relative providers as defined in WAC 170-290-0003(13), and for all licensed family homes.
- (2) The responsibilities of the department of social and health services (DSHS) include, but are not limited to:
 - (a) Service delivery for the WCCC and SCC programs, including determining who is eligible for WCCC and SCC benefits; and

WAC 170-290-0268, Payment discrepancies—Provider overpayments, states:

- (1) An overpayment occurs when a provider receives payment that is more than the provider is eligible to receive. Provider overpayments are established when that provider:
 - (a) Bills and receives payment for services not provided;
 - (b) Bills without attendance records that support their billing;
 - (c) Bills and receives payment for more than they are eligible to bill;
 - (d) Routinely provides care in a location other than what was approved at the time of authorization;
 - (e) With respect to license-exempt in-home/relative providers, commonly known as "family, friends, and neighbor" providers, bills the state for more than six children at one time during the same hours of care; or
 - (f) With respect to licensed or certified providers:
 - (i) Bills the state for more than the number of children they have in their licensed capacity; or
 - (ii) Is caring for a WCCC child outside their licensed allowable age range without a DEL-approved exception; or
 - (g) With respect to certified providers caring for children in a state bordering Washington:

- (i) Is determined not to be in compliance with their state's licensing regulations;
or
- (ii) Fails to notify DSHS within ten days of any suspension, revocation, or change to their license.
- (2) DEL or DSHS will request documentation from a provider when preparing to establish an overpayment. The provider has twenty-eight consecutive calendar days from the date of the written request to supply any requested documentation.
- (3) A provider is required to repay any payments which they were not eligible to receive.
- (4) Provider overpayments defined in subsection (1) of this section are deemed as program violations as described in WAC 170-290-0277.
- (5) A provider is required to repay any overpayment made through a departmental error.

WAC 170-290-0271 Payment discrepancies—Consumer overpayments, states:

- (1) DSHS establishes overpayments for past or current consumers when the consumer:
 - (a) Received benefits in an amount greater than the consumer was eligible to receive;
 - (b) Is determined eligible at application or reapplication based on the consumer's participation in an approved activity and used benefits, but never participated in said activity;
 - (c) Failed to report changes under the requirements of WAC 170-290-0031 to DSHS which result in an error in determining eligibility, amount of care authorized, or copayment;
 - (d) Used a provider who did not meet the eligibility requirements under WAC 170-290-0125;
 - (e) Received benefits for a child who was not eligible per WAC 170-290-0005, 170-290-0015 or 170-290-0020; or
 - (f) Failed to return, by the sixtieth day, the requested income verification of new employment as provided in WAC 170-290-0012.
- (2) DEL or DSHS may request documentation from a consumer when preparing to establish an overpayment. The consumer has fourteen consecutive calendar days to supply any requested documentation.
- (3) Consumers are required to repay any benefits paid by DSHS that they were not eligible to receive.

WAC 170-290-0030 Consumers' responsibilities, states in part:

When a person applies for or receives WCCC benefits, the applicant or consumer must, as a condition of receiving those benefits:

- (11) Document their child's attendance in child care by having the consumer or other person authorized by the consumer to take the child to or from the child care:
 - (a) If the provider uses a paper attendance record, sign the child in on arrival and sign the child out at departure, using their full signature and writing the time of arrival and departure; or
 - (b) Record the child's attendance using an electronic system if used by the provider;

WAC 170-290-0034 Providers' responsibilities, states:

Child care providers who accept child care subsidies must do the following:

- (1) Comply with:
 - (a) All of the DEL child care licensing or certification requirements as provided in chapter 170-295, 170-296A, or 170-297 WAC, for child care providers who are licensed or certified; or
 - (b) All of the requirements in WAC 170-290-0130 through 170-290-0167, 170-290-0250, and 170-290-0268, for child care providers who provide in-home/relative care;
- (2) Report pending charges or convictions to DSHS as provided in:
 - (a) Chapter 170-295, 170-296A, or 170-297 WAC, for child care providers who are licensed or certified; or
 - (b) WAC 170-290-0138 (2) and (3), for child care providers who provide in-home/relative care;
- (3) Keep complete and accurate daily attendance records for children in their care, and allow access to DEL to inspect attendance records during all hours in which authorized child care is provided as follows:
 - (a) Current attendance records (including records from the previous twelve months) must be available immediately for review upon request by DEL.
 - (b) Attendance records older than twelve months to five years must be provided to DSHS or DEL within two weeks of the date of a written request from either department. Beginning July 1, 2017, or upon ratification of the 2017-19 collective bargaining agreement with SEIU 925, whichever occurs later, the records must be provided within twenty-eight consecutive calendar days of the date of a written request from either department.
 - (c) Failure to make available attendance records as provided in this subsection may:
 - (i) Result in the immediate suspension of the provider's subsidy payments; and
 - (ii) Establish a provider overpayment as provided in WAC 170-290-0268;
- (4) Keep receipts for billed field trip/quality enhancement fees as follows:
 - (a) Receipts from the previous twelve months must be available immediately for review upon request by DEL;
 - (b) Receipts from one to five years old must be provided to DSHS or DEL within two weeks of the date of a written request from either department;
- (5) Allow consumers access to their child at all times while the child is in care;
- (6) Collect copayments directly from the consumer or the consumer's third-party payor, and report to DSHS if the consumer has not paid a copayment to the provider within the previous sixty days;
- (7) Follow billing procedures:
 - (a) As described in the most current version of "Child Care Subsidies: A Guide for Licensed and Certified Family Home Child Care Providers,"; or
 - (b) As described in the most current version of "Child Care Subsidies: A Guide for Family, Friends and Neighbors Child Care Providers"; or
 - (c) As described in the most current version of "Child Care Subsidies: A Guide for Licensed and Certified Child Care Centers."
- (8) Not claim a payment in any month a child has not attended at least one day within the authorization period in that month.

- (9) Invoice the state no later than one calendar year after the actual date of service;
- (10) For both licensed and certified providers and in-home/relative providers, not charge subsidized families the difference between the provider's customary rate and the maximum allowed state rate; and
- (11) For licensed and certified providers, not charge subsidized families for:
 - (a) Registration fees in excess of what is paid by subsidy program rules;
 - (b) Absent days on days in which the child is scheduled to attend and authorized for care;
 - (c) Handling fees to process consumer copayments, child care services payments, or paperwork;
 - (d) Fees for materials, supplies, or equipment required to meet licensing rules and regulations; or
 - (e) Child care or fees related to subsidy billing invoices that are in dispute between the provider and the state.

WAC 170-290-0138 In-home/relative providers—Responsibilities, states in part:

An in-home/relative provider must:

- (6) Bill only for actual hours of care provided. Those hours:
 - (a) Must be authorized by DSHS;
 - (b) Must be used by the consumer; and
 - (c) Can be claimed whether or not the consumer is present during the hours of care.
- (7) Bill for no more than six children at one time during the same hours of care;
- (8) Track attendance documenting the days and hours of care provided and keep records for five years:
 - (a) If paper attendance records are used, the provider must have the consumer sign and date the attendance records at least weekly, verifying the accuracy of the dates and times. (b) Providers may use an electronic attendance system as provided in WAC 170-290-0139 to record attendance in lieu of a paper sign-in record;
- (9) Repay any overpayments under WAC 170-290-0268; and

WAC 170-290-0190 WCCC benefit calculations, states:

- (1) The amount of care a consumer may receive is determined by DSHS at application or reapplication. The consumer does not need to be in approved activities or a reported activity schedule, except at application or reapplication. Once the care is authorized, the amount will not be reduced during the eligibility period unless:
 - (a) The consumer requests the reduction;
 - (b) The care is for a school-aged child as described in subsection (3) of this section; and
 - (c) Incorrect information was given at application or reapplication according to WAC 170-290-0030.
- (2) To determine the amount of weekly hours of care needed, DSHS will review:
 - (a) The consumer's participation in approved activities per WAC 170-290-0040, 170-290-0045, 170-290-0050, and 170-290-0055;
 - (b) The number of hours the child attends school, including home school, and reduce the amount of care;

- (c) In a two parent household, the days and times the activities overlap, and only authorize care during those times;
 - (d) The parent, in a two parent household, who is not able to care for the child, as defined in WAC 170-290-0020, and exclude the activity requirements; and
 - (e) When a consumer requests and verifies the need for increased care, DSHS will increase the care for the remainder of the eligibility period.
- (3) Determining full-time care for a family using licensed providers:
- (a) Twenty-three full-day units per month will be authorized for one hundred ten hours of activity or more each month when the child needs care five or more hours per day;
 - (b) Thirty half-day units per month will be authorized for one hundred ten hours of activity or more each month when the child needs care less than five hours per day;
 - (c) Thirty half-day units per month will be authorized during the school year for a school-aged child who needs care less than five hours per day;
 - (d) Forty-six half-day units will be authorized during the months of July and August for a school-aged child who needs five or more hours of care;
 - (e) Twenty-three full-day units will be authorized during the school year for a school-aged child who needs care five or more hours per day;
 - (f) Supervisor approval is required for additional days of care that exceeds twenty-three full days or thirty half days; and
 - (g) Care cannot exceed sixteen hours per day, per child.
- (4) Determining full-time care for a family using in-home/relative providers (family, friend and neighbors).
- (a) Two hundred thirty hours of care will be authorized for one hundred ten hours of activity or more each month when the child needs care five or more hours per day;
 - (b) One hundred fifteen hours of care will be authorized for one hundred ten hours of activity or more each month when the child needs care less than five hours per day;
 - (c) One hundred fifteen hours of care will be authorized during the school year for a school-aged child who needs care less than five hours per day and the provider will be authorized contingency hours each month, up to a maximum of two hundred thirty hours;
 - (d) Two hundred thirty hours of care will be authorized during the school year for a school-aged child who needs care five or more hours in a day;
 - (e) Supervisor approval is required for hours of care that exceed two hundred thirty hours; and
 - (f) Care cannot exceed sixteen hours per day, per child.
- (5) Determining part-time care for a family using licensed providers and the activity is less than one hundred ten hours per month.
- (a) A full-day unit will be authorized for each day of care that exceeds five hours;
 - (b) A half-day unit will be authorized for each day of care that is less than five hours; and
 - (c) A half-day unit will be authorized for each day of care for a school-aged child, not to exceed thirty half days.
- (6) Determining part-time care for a family using in-home/relative providers (family, friend and neighbors).

- (a) Under the provisions of subsection (2) of this section, DSHS will authorize the number of hours of care needed per month when the activity is less than one hundred ten hours per month; and
- (b) When the provider claims contingency hours, the total number of authorized hours and contingency hours claimed cannot exceed two hundred thirty hours per month.
- (7) DSHS determines the allocation of hours or units for families with multiple providers based upon the information received from the parent.
- (8) DSHS may authorize more than the state rate and up to the provider's private pay rate if:
 - (a) The parent is a WorkFirst participant; and
 - (b) Appropriate child care, at the state rate, is not available within a reasonable distance from the approved activity site. "Appropriate" means licensed or certified child care under WAC 170-290-0125, or an approved in-home/relative provider under WAC 170-290-0130. "Reasonable distance" is determined by comparing distances other local families must travel to access appropriate child care.
- (9) Other fees DSHS may authorize to a provider are:
 - (a) Registration fees;
 - (b) Field trip fees;
 - (c) Nonstandard hours bonus;
 - (d) Overtime care to a licensed provider who has a written policy to charge all families, when care is expected to exceed ten hours in a day; and
 - (e) Special needs rates for a child.
- (10) In-home/relative providers who are paid child care subsidies to care for children receiving WCCC benefits cannot receive those benefits for their own children during the hours in which they provide subsidized child care.

WAC 170-290-0245 Registration fees, states:

- (1) DSHS may pay licensed or certified child care providers and DEL contracted seasonal day camps a registration fee when:
 - (a) A child is first enrolled by the consumer for child care with a provider;
 - (b) A consumer enrolls their child with a new child care provider during their eligibility period; or
 - (c) A child has more than a sixty-day break in child care services with the same provider, and it is the provider's policy to charge all parents this fee when there is a break in service.
- (2) A registration fee will be paid only once per calendar year for children who are cared for by the same provider, even if the provider receives subsidy payments under different subsidy programs during this time period for the enrolled children, unless there is a break of sixty days or more as provided in subsection (1)(c) of this section.

WAC 170-290-0247 Field trip/quality enhancement fees, states:

- (1) DSHS pays licensed or certified family home child care providers a monthly field trip/quality enhancement fee up to thirty dollars per child or the provider's actual cost for the field trip, whichever is less, only if the fee is required of all parents whose children are in the provider's care. DEL-licensed or certified child care centers and school-age centers are not eligible to receive the field trip/quality enhancement fee.

- (2) The field trip/quality enhancement fee is to cover the provider's actual expenses for:
 - (a) Admission;
 - (b) Enrichment programs and/or ongoing lessons;
 - (c) Public transportation or mileage reimbursement at the state office of financial management rate for the use of a private vehicle;
 - (d) The cost of hiring a nonemployee to provide an activity at the child care site in-house field trip activity; and
 - (e) The purchase or development of a prekindergarten curriculum.
- (3) The field trip/quality enhancement fee shall not cover fees or admission costs for adults on field trips, or food purchased on field trips.

WAC 170-290-0249 Nonstandard hours bonus, states:

- (1) A consumer's provider may receive a nonstandard hours bonus (NSHB) payment of seventy-five dollars per child per month for care provided if:
 - (a) The provider is licensed or certified;
 - (b) The provider provides at least thirty hours of non- standard hours care during one month; and
 - (c) The total cost of the NSHB to the state does not exceed the amount appropriated for this purpose by the legislature for the current state fiscal year.
- (2) Nonstandard hours are defined as:
 - (a) Before 6 a.m. or after 6 p.m.;
 - (b) Any hours on Saturdays and Sundays; and
 - (c) Any hours on legal holidays, as defined in RCW 1.16.050.

2018-027

The Department of Social and Health Services did not have adequate internal controls over maintenance of effort requirements for the Temporary Assistance for Needy Families grant.

Federal Awarding Agency: U.S. Department of Health and Human Services
Pass-Through Entity: None
CFDA Number and Title: 93.558 Temporary Assistance for Needy Families
Federal Award Number: 1701WATANF, 1701WATAN3, 1801WATANF, 1801WATAN3
Applicable Compliance Component: Level of Effort
Known Questioned Cost Amount: None

Background

The Department of Social and Health Services (Department), Community Services Division, administers the Temporary Assistance for Needy Families (TANF) grant that provides temporary cash assistance for families in need. The Department spent more than \$326 million in federal grant funds during fiscal year 2018.

Federal regulations require the Department to maintain state spending at certain levels to meet federal grant requirements, referred to as maintenance of effort (MOE). The state must:

- Maintain state expenditures for eligible families at a level that is at least 80 percent of historical state expenditures.
- Maintain state expenditures at a level that is more than 100 percent of its historical state expenditures for fiscal year 1994 to keep any of the federal contingency funding it received.
- Maintain supporting documentation to show the state is complying with MOE requirements.

Although the Department administers the grant, it can count certain expenditures made by other state agencies and nonprofit organizations toward its MOE requirements. The Department must ensure these expenditures of other agencies and organizations were for TANF-eligible clients.

During state fiscal year 2018, the Department claimed about \$183 million of its own spending in eight programs toward its MOE requirements. In addition, the Department claimed about \$443 million of expenditures from another 15 programs, including six other state agencies and two nonprofit organizations. These expenditures were not part of the state's TANF program.

The Department uses information from large databases to produce a list of TANF MOE eligible clients to make determinations about client status and client TANF MOE eligibility. Other agencies use this list to identify state funds paid for benefits provided to the same clients. The Department's codes for this process are used year after year.

In our last three audits, we reported the Department did not have adequate internal controls to ensure it complied with the MOE requirements. These were reported as finding numbers 2017-019, 2016-017 and 2015-020.

Description of Condition

The Department did not have adequate internal controls in place to ensure it complied with the MOE requirements.

We observed no evidence to support that the Department's codes were independently reviewed. Additionally, there is no formal documentation or tracking of requests detailing what coding changes were implemented. Department staff said versions of codes are manually saved so there is a history, but without automated version control, or an alternative method, there is an increased risk that changes to code could be made and not reviewed.

We also found the Department did not:

- Adequately monitor expenditures throughout the year to ensure it would meet the MOE expenditure level requirements
- Review final expenditure data from outside agencies to determine whether the expenditures were allowable and adequately supported

We consider these internal control weaknesses to be a significant deficiency. We were able to examine other supporting data not used by the report preparers to gain reasonable assurance the amounts reported by the Department were materially accurate.

Cause of Condition

The Department did not have adequate written policies and procedures in place to ensure it complied with MOE requirements. Additionally, management did not adequately monitor to ensure the Department complied with federal requirements because it believed testing a sample of cases along with informal review and testing of coding changes were sufficient to ensure accuracy and completeness.

The Department did not have ongoing fiscal monitoring to ensure it met the MOE requirements. The Department believed that using budget data for the corresponding fiscal year would ensure it met MOE requirements. However, having sufficient budget does not provide assurance that funds were properly spent.

The Department believed it could rely on the other agencies' processes to ensure additional MOE expenditures were allowable, supported and correct, through the use of attestations that accompany emails stating amounts spent.

Effect of Condition

By not performing adequate reviews of coding and expenditure data, the Department cannot ensure expenditures claimed as MOE were allowable.

The Department did not know if it would be compliant with MOE requirements until after the year had ended because it did not perform ongoing monitoring.

Although we determined the Department was materially compliant with the MOE requirements, we found:

- \$286 in unallowable expenditures were counted as MOE. Our examination was performed using a statistically valid sampling method. We estimate the Department claimed a total of \$191,286 in unallowable expenditures.
- \$86,785 in expenditures were already used for another federal match and improperly counted as MOE.

If it does not ensure the data is allowable and accurate, the Department could unknowingly become noncompliant, and the grantor could reduce future grant funds in the amount of the shortage.

Recommendations

We recommend the Department establish adequate internal controls to ensure it:

- Tracks changes made to code and keeps records to show who made the changes
- Performs and documents independent reviews of code changes
- Establishes written policies or procedures that describe the roles and responsibilities of staff who make coding changes and management who review the changes
- Establishes written policies and procedures that describe the complex process used to collect and review documentation to support MOE expenditures
- Monitors expenditure levels throughout the fiscal year to ensure MOE requirements are being met

Department's Response

The Department partially concurs with the overall findings of the State Auditor's Office (SAO).

The Department partially concurs it did not have adequate written policies and procedures in place. The Department developed manuals that outline collaborative report preparation procedures between the Community Services Division, the Research and Data Analysis Division, and the Division of Finance and Financial Recovery which were effective February 1, 2017. In response to audit findings 2017-018 and 2017-020, the Department continued to host weekly TANF MOE workgroup meetings in which members would review and update policies and procedures related to MOE expenditures to address the previously identified internal control weaknesses. However, these changes were not fully implemented until March 2018, about three quarters of the way through the audit period.

The Department does not concur that it did not have ongoing fiscal monitoring to ensure it met the MOE requirements. In response to audit findings 2017-018 and 2017-020, the Department implemented the use of Memorandums of Understanding (MOUs) at the beginning of each year to ensure the previous year's sources are viable for the current fiscal year. The MOUs give the Department the opportunity to discuss current program operations, allowable activities and expenditures, and develop a projection of expenditures with the partnering source. During

presentation of the MOU, the Department also reviews partners' methodologies and record management protocols, and offers training and assistance, if needed.

Effective March 1, 2018, the Department implemented a quarterly monitoring/reporting schedule with representatives from the Community Services Division, Division of Finance and Financial Recovery, and the Research and Data Analysis Division to ensure reported expenditures from all MOE sources are allowable and accurate in a timelier manner, and to review expenditure projections. The Department's use of MOUs during the first quarter of the corresponding federal fiscal year, and the improved review/reporting schedule, allows the Department to forecast and monitor its ability to meet both its TANF MOE and TANF Contingency Fund requirements throughout the year.

The Department does not concur with SAOs statement, "The Department believed that using budget data for the corresponding fiscal year would ensure it met MOE requirements. However, having sufficient budget does not provide assurance that funds were properly spent." The Department does not review previous budget data, but rather reviews budget data for upcoming years. The Department conducts a trend analysis with previous years' data to ensure the budget is similar to years prior, however, this is only one method in which the Department ensures it will meet the MOE requirements. The Department also submits quarterly 196R financial reports, which contain Departmental MOE expenditures. Furthermore, the Department verifies through written agreements with each source at the outset of the FFY that, to the best of the partner's ability, the source will have eligible programs and similar expenditure levels to prior reports.

The Department does not concur with SAOs statement that "The Department believed it could rely on the other agencies' processes to ensure additional MOE expenditures were allowable, supported and correct, through the use of attestations that accompany emails stating amounts spent." The Department uses data exchange methods between each partnering agency to ensure expenditures are verifiable, allowable, and accurate to the best of its ability while respecting client data sensitivities. The Department ensures expenditures are verifiable, allowable, and accurate by using the aforementioned MOUs, in addition to in-person meetings at the outset of the federal fiscal year (FFY), monitoring practices throughout the year, data exchanges between the agencies and DSHS, and by requiring attestations from partnering sources when final figures are reported.

Out of 11 partnering sources, there are only three outside agencies, Labor and Industries, The Department of Children, Youth, and Families, and the Office of the Superintendent of Public Instruction, with protected data sources in which client identifiers are not exchanged. As documented in the Department's procedure manuals, these sources participate in the Department's data exchange methods to the best of their abilities, with client identifiers omitted, to ensure expenditures are allowable, accurate, and verifiable.

The Department's Research and Data Analysis Division does not concur with SAOs statement that "management did not adequately monitor to ensure the Department complied with federal requirements because it believed testing a sample of cases along with informal review and testing of coding changes were sufficient to ensure accuracy and completeness." The Department believes that the formal testing processes executed and documented during fiscal year 2018 were sufficient to ensure it complied with MOE requirements. However, the Department concurs that SAOs suggestions will improve the process and will incorporate the suggestions into its practices.

Auditor’s Concluding Remarks

We were provided evidence to show the Department held workgroup meetings and implemented quarterly processes during the audit period, but they did not impact the Department’s reporting for federal fiscal year 2017.

Additionally, both program staff and RDA staff confirmed that, other than an excel spreadsheet showing totals and a certification, no further supporting documentation was received by the Department to confirm the expenditures that were claimed, how the calculations were performed or if the totals were reviewed prior to being sent to the Department.

Without the use of a program change tool, or alternative method, to identify what code was modified, added or deleted, there is an increased risk that changes to code could be made, either intentionally or unintentionally, and not reviewed. This created an internal control weakness that affects the data match process with the other agencies the Department claims MOE expenditures from.

We reaffirm our finding and will review the status of the Department’s corrective action during our next audit.

Applicable Laws and Regulations

Title 2 U.S. Code of Federal Regulations Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance) establishes the following applicable requirements:

Section 200.303 Internal controls, states in part:

The non-Federal entity must:

- (a) Establish and maintain effective internal control over the Federal award that provides reasonable assurance that the non-Federal entity is managing the Federal award in compliance with Federal statutes, regulations, and the terms and conditions of the Federal award. These internal controls should be in compliance with guidance in “Standards for Internal Control in the Federal Government” issued by the Comptroller General of the United States or the “Internal Control Integrated Framework”, issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).

Section 200.516 Audit findings, states in part:

- (a) *Audit findings reported.* The auditor must report the following as audit findings in a schedule of findings and questioned costs:
 - (1) Significant deficiencies and material weaknesses in internal control over major programs and significant instances of abuse relating to major programs. The auditor’s determination of whether a deficiency in internal control is a significant deficiency or material weakness for the purpose of reporting an audit finding is in relation to a type of compliance requirement for a major program identified in the Compliance Supplement.

The American Institute of Certified Public Accountants defines significant deficiencies and material weaknesses in internal controls over compliance in its *Codification of Statements on Auditing Standards*, section 935, Compliance Audits, as follows:

.11 For purposes of adapting GAAS to a compliance audit, the following terms have the meanings attributed as follows: ...

Deficiency in internal control over compliance. A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance on a timely basis. A deficiency in design exists when (a) a control necessary to meet the control objective is missing, or (b) an existing control is not properly designed so that, even if the control operates as designed, the control objective would not be met. A deficiency in operation exists when a properly designed control does not operate as designed or the person performing the control does not possess the necessary authority or competence to perform the control effectively.

Material weakness in internal control over compliance. A deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a compliance requirement will not be prevented, or detected and corrected, on a timely basis. In this section, a reasonable possibility exists when the likelihood of the event is either reasonably possible or probable as defined as follows:

Reasonably possible. The chance of the future event or events occurring is more than remote but less than likely.

Probable. The future event or events are likely to occur.

Significant deficiency in internal control over compliance. A deficiency, or a combination of deficiencies, in internal control over compliance that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

45 Code of Federal Regulation section 263 Expenditures of State and Federal TANF Funds, states in part

Section 263.1 – How much State money must a State expend annually to meet the basic MOE requirement, states in part:

(a) (1) The minimum basic MOE for a fiscal year is 80 percent of a State’s historic State expenditures.

Section 263.2 – What kinds of State expenditures count toward meeting a State’s basic MOE expenditure requirement, states in part:

(e) Expenditures for benefits or services listed under paragraph (a) of this section may include allowable costs borne by others in the State (e.g., local government), including cash donations from non-Federal third parties (e.g., a non-profit organization) and the value of third party in-kind contributions if:

(1) The expenditure is verifiable and meets all applicable requirements in 45 CFR 92.3 and 92.24;

(2) There is an agreement between the State and the other party allowing the State to count the expenditure toward its MOE requirement; and,

(3) The State counts a cash donation only when it is actually spent.

Section 263.8 - What happens if a State fails to meet the basic MOE requirement?

- (a) If any State fails to meet its basic MOE requirement for any fiscal year, then we will reduce dollar-for-dollar the amount of the SFAG payable to the State for the following fiscal year.
- (b) If a State fails to meet its basic MOE requirement for any fiscal year, and the State received a WtW formula grant under section 403(a)(5)(A) of the Act for the same fiscal year, we will also reduce the amount of the SFAG payable to the State for the following fiscal year by the amount of the WtW formula grant paid to the State.

Section 263.9 May a State avoid a penalty for failing to meet the basic MOE requirement through reasonable cause or corrective compliance?

No. The reasonable cause and corrective compliance provisions at §§ 262.4, 262.5, and 262.6 of this chapter do not apply to the penalties in § 263.8.

Section 264.72 What requirements are imposed on a State if it receives contingency funds, states in part:

- (a) (1) A State must meet a Contingency Fund MOE level of 100 percent of historic State expenditures for FY 1994.
- (2) A State must exceed the Contingency Fund MOE level to keep any of the contingency funds that it received. It may be able to retain a portion of the amount of contingency funds that match countable State expenditures, as defined in § 264.0, that are in excess of the State's Contingency Fund MOE level, after the overall adjustment required by section 403(b)(6)(C) of the Act.

2018-028

The Department of Social and Health Services did not have adequate internal controls in place to ensure quarterly reports for the Temporary Assistance for Needy Families Grant were submitted accurately.

Federal Awarding Agency: U.S. Department of Health and Human Services
Pass-Through Entity: None
CFDA Number and Title: 93.558 Temporary Assistance for Needy Families
Federal Award Number: 1701WATANF, 1701WATAN3, 1801WATANF, 1801WATAN3
Applicable Compliance Component: Reporting
Known Questioned Cost Amount: None

Background

The Department of Social and Health Services, Community Services Division (Department), administers the Temporary Assistance for Needy Families (TANF) grant that provides temporary cash assistance for families in need. To receive TANF benefits, participants must be engaged in entering the work force through the Work First program, with limited exceptions. State agencies must meet or exceed minimum annual work participation rates of 50 percent overall and 90 percent for two parents. The Department spent more than \$326 million in grant funds during fiscal year 2018.

Federal regulations require the Department to file quarterly reports that include work participation data at summary and individual levels. The Department must file separate reports for its federal TANF program and state programs. The proper reporting of work participation data is critical because it serves as the basis for the federal government's determination of whether states have met the required work participation rates. A penalty may apply for failure to meet the required rates.

In prior audits, we reported the Department did not have adequate internal controls in place to ensure quarterly reports were submitted accurately. The prior finding numbers were 2017-020 and 2016-016.

Description of Condition

The Department did not have adequate internal controls in place to ensure quarterly reports were prepared accurately. Data is extracted from large databases and then transformed with customized code to produce the amounts cited in the reports. The Department performed informal, manual reviews in an attempt to ensure coding changes were applied properly. We found these reviews were not adequate to ensure all changes were properly identified and reviewed. Additionally, the reviews were not sufficiently documented. For these reasons, we could not evaluate if internal controls were in place and effective.

In addition, the customized code was established years ago and continued to be used during the audit period. The Department could not provide evidence to support the code was independently reviewed to ensure that the parameters are still valid.

When existing code needs to be changed or new code is added, staff from the TANF program and other programs managed by DSHS are involved in the decision process. This collaboration happens during meetings and email communications. There was no formal documentation or tracking of requests. If there is review, it was not documented so we could not verify whether the control was in place and operating effectively. Without an automated process to monitor these changes in code, the Department cannot ensure all changes were authorized.

We consider these internal control weaknesses to constitute a significant deficiency. We were able to examine other supporting data not used by the report preparers to verify the amounts reported by the Department were materially accurate.

Cause of Condition

Management believed its informal review and testing of new coding was sufficient to ensure accuracy and completeness of the data. Written policies or procedures regarding the process for making changes to code and reviewing those changes have not been implemented.

Effect of Condition

Because it did not perform adequate reviews, the Department cannot ensure data used for reporting purposes was accurate. The Department could become noncompliant with grant terms, which would allow the grantor to penalize the Department 4 percent of the grant for each quarter if the state fails to submit accurate, complete and timely reports, and up to 21 percent for not meeting minimum participation rates.

Recommendations

We recommend the Department establish adequate internal controls to ensure:

- Changes made to code are tracked and records indicate who made the changes
- Independent reviews of code changes are performed and documented
- Establish written policies or procedures that describe the roles and responsibilities of staff who make coding changes and management who review the changes

Department's Response

The Department partially agrees with the audit finding.

The Department concurs:

- *Written policies and procedures that describe how the Department ensures grant reporting data is accurate and complete needs to be sufficient.*
 - *While the Department documented the 199 and 209 processes in detail, the Department continues to extend and update documentation and written policies and procedures for this complex reporting process.*
- *Internal controls are needed to ensure accuracy and completeness.*

- *The Department has extensive documentation on algorithms for deriving the items in the federal transmission, including specifications on tables and codes in the Automated Client Eligibility System (ACES) and the Social Service Payment System (SSPS) and how Statistical Analysis System (SAS) processes use these data to comply with reporting requirements. Staff also run a quality assurance process for each report that identifies potential fatal and warning edits; these results are reviewed by the Supervisor. The Department believes controls for change requests, coding updates and the approval processes are adequate.*
- *The Department implemented a quarterly internal control/quality assurance process beginning in January 2017. In this process, a random sample of 199 and 209 reported cases are checked against the source data systems for correctness, and a summary of the quality assurance results are reviewed by a supervisor.*
- *While the Department may benefit from a more formal process, the review of both code and results is extensive and the process includes monthly dissemination of summary data to multiple partners for review and validation. The quarterly reports required for meeting participation rates were accurate, complete and submitted timely.*

The Department does not concur change control software is required.

- *Manual monitoring, reviewing, and testing of coding changes were performed by Department staff to ensure they were applied correctly. While no version control software was used by the Department, staff kept systematic copies of all old code versions using filename conventions, duplicating most of the functionality of version control software. The Department is not aware of any audit standards that require version control software to be used by entities audited under the Single Federal Audit.*

The Department will ensure:

- *Quarterly quality assurance testing using statistical sampling continues to be performed in order to ensure that “data used for reporting purposes was accurate and complete.”*
- *Written policies and procedures will continue to be updated that describe “how the Department ensures the reported data is accurate and complete.”*
- *Written policies and procedures will be developed and implemented to reinforce the need of thorough documentation of code review, testing, and approval before moving code changes into the production environment.*

Auditor’s Concluding Remarks

Without the use of a program change tool, or alternative method, to identify what code was modified, added or deleted, there is an increased risk that changes to code could be made, either intentionally or unintentionally, and not reviewed.

We reaffirm our finding and will review the status of the Department’s corrective action during our next audit.

Applicable Laws and Regulations

Title 2 U.S. Code of Federal Regulations Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance) establishes the following applicable requirements:

Section 200.303 Internal controls, states in part:

The non-Federal entity must:

- (a) Establish and maintain effective internal control over the Federal award that provides reasonable assurance that the non-Federal entity is managing the Federal award in compliance with Federal statutes, regulations, and the terms and conditions of the Federal award. These internal controls should be in compliance with guidance in “Standards for Internal Control in the Federal Government” issued by the Comptroller General of the United States or the “Internal Control Integrated Framework”, issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).

Section 200.516 Audit findings, states in part:

- (a) *Audit findings reported.* The auditor must report the following as audit findings in a schedule of findings and questioned costs:
 - (1) Significant deficiencies and material weaknesses in internal control over major programs and significant instances of abuse relating to major programs. The auditor’s determination of whether a deficiency in internal control is a significant deficiency or material weakness for the purpose of reporting an audit finding is in relation to a type of compliance requirement for a major program identified in the Compliance Supplement.

The American Institute of Certified Public Accountants defines significant deficiencies and material weaknesses in internal controls over compliance in its *Codification of Statements on Auditing Standards*, section 935, Compliance Audits, as follows:

.11 For purposes of adapting GAAS to a compliance audit, the following terms have the meanings attributed as follows: ...

Deficiency in internal control over compliance. A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance on a timely basis. A deficiency in design exists when (a) a control necessary to meet the control objective is missing, or (b) an existing control is not properly designed so that, even if the control operates as designed, the control objective would not be met. A deficiency in operation exists when a properly designed control does not operate as designed or the person performing the control does not possess the necessary authority or competence to perform the control effectively.

Material weakness in internal control over compliance. A deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a compliance requirement will not be prevented, or detected and corrected, on a timely basis. In this section, a reasonable possibility exists when

the likelihood of an event occurring is either reasonably possible or probable as defined as follows:

Reasonably possible. The chance of the future event or events occurring is more than remote but less than likely.

Probable. The future event or events are likely to occur.

Significant deficiency in internal control over compliance. A deficiency, or a combination of deficiencies, in internal control over compliance that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

Title 45, Code of Federal Regulations

Section 265.3 – What reports must the State file on a quarterly basis, states in part:

- (a) Quarterly reports
 - (1) Each State must collect on a monthly basis, and file on a quarterly basis, the data specified in the TANF Data Report and the TANF Financial Report
 - (2) Each State that claims MOE expenditures for a separate State program(s) must collect on a monthly basis, and file on a quarterly basis, the data specified in the SSP-MOE Data Report.
- (b) *TANF Data Report.* The TANF Data Report consists of four sections. Two sections contain disaggregated data elements and two sections contain aggregated data elements.
 - (1) *Disaggregated Data on Families Receiving TANF Assistance – Section one.* Each State must file disaggregated information on families receiving TANF assistance. This section specifies identifying and demographic data such as the individual’s Social Security Number and information such as the amount of assistance received, educational level, employment status, work participation activities, citizenship status, and earned and unearned income. The data must be provided by both adults and children.
 - (2) *Disaggregated Data on Families No Longer Receiving TANF Assistance - Section two.* Each State must file disaggregated information on families no longer receiving TANF assistance. This section specifies the reasons for case closure and data similar to the data required in section one.
 - (3) *Aggregated Data - Section three.* Each State must file aggregated information on families receiving, applying for, and no longer receiving TANF assistance. This section of the TANF Data Report requires aggregate figures in such areas as: The number of applications received and their disposition; the number of recipient families, adult recipients, and child recipients; the number of births and out-of-wedlock births for families receiving TANF assistance; the number of noncustodial parents participating in work activities; and the number of closed cases.
 - (4) *Aggregated Caseload Data by Stratum-Section four.* Each State that opts to use a stratified sample to report the quarterly TANF disaggregated data must file the monthly caseload data by stratum for each month in the quarter.
- (d) *SSP-MOE Data Report.* The SSP-MOE Data Report consists of four sections. Two sections contain disaggregated data elements and two sections contain aggregated data elements.

- (1) *Disaggregated Data on Families Receiving SSP-MOE Assistance - Section one.* Each State that claims MOE expenditures for a separate State program(s) must file disaggregated information on families receiving SSP-MOE assistance. This section specifies identifying and demographic data such as the individual's Social Security Number, the amount of assistance received, educational level, employment status, work participation activities, citizenship status, and earned and unearned income. The data must be provided for both adults and children.
- (2) *Disaggregated Data on Families No Longer Receiving SSP-MOE Assistance - Section two.* Each State that claims MOE expenditures for a separate State program(s) must file disaggregated information on families no longer receiving SSP-MOE assistance. This section specifies the reasons for case closure and data similar to the data required in section one.
- (3) *Aggregated Data - Section three.* Each State that claims MOE expenditures for a separate State program(s) must file aggregated information on families receiving and no longer receiving SSP-MOE assistance. This section of the SSP-MOE Data Report requires aggregate figures in such areas as: The number of recipient families, adult recipients, and child recipients; the total amount of assistance for families receiving SSP-MOE assistance; the number of non-custodial parents participating in work activities; and the number of closed cases.
- (4) *Aggregated Caseload Data by Stratum - Section four.* Each State that claims MOE expenditures for a separate State program(s) and that opts to use a stratified sample to report the SSP-MOE quarterly disaggregated data must file the monthly caseload by stratum for each month in the quarter.
- (e) *Optional data elements.* A State has the option not to report on some data elements for some individuals in the TANF Data Report and the SSP-MOE Data Report, as specified in the instructions to these reports.
- (f) *Non-custodial parents.* A State must report information on a non-custodial parent (as defined in § 260.30 of this chapter) if the non-custodial parent:
 - (1) Is receiving assistance as defined in § 260.31 of this chapter;
 - (2) Is participating in work activities as defined in section 407(d) of the Act; or
 - (3) Has been designated by the State as a member of a family receiving assistance.

Title 45, Code of Federal Regulations

Section 262.1 What penalties apply to States [states in part]?

- (a) We will assess fiscal penalties against States under circumstances defined in parts 261 through 265 of this chapter. The penalties are:
 - (1) A penalty of the amount by which a State misused its TANF funds;
 - (2) An additional penalty of five percent of the adjusted SFAG if such misuse was intentional;
 - (3) A penalty of four percent of the adjusted SFAG for each quarter a State fails to submit an accurate, complete and timely required report;
 - (4) A penalty of up to 21 percent of the adjusted SFAG for failure to satisfy the minimum participation rates;

2018-029

The Department of Social and Health Services did not have adequate internal controls in place for submitting quarterly and annual reports for the Temporary Assistance for Needy Families grant.

Federal Awarding Agency: U.S. Department of Health and Human Services
Pass-Through Entity: None
CFDA Number and Title: 93.558 Temporary Assistance for Needy Families
Federal Award Number: 1701WATANF;1801WATANF;1701WATAN3;
1801WATAN3
Applicable Compliance Component: Reporting
Known Questioned Cost Amount: None

Background

The Department of Social and Health Services (Department), Community Services Division, administers the Temporary Assistance for Needy Families (TANF) grant that provides temporary cash assistance for families in need. To receive TANF benefits, participants must be engaged in entering the work force through the Work First program, with limited exceptions.

The Department spent about \$326 million in federal grant funds during state fiscal year 2018. In addition, the Department reported it spent about \$626 million in state funds toward meeting a maintenance of effort (MOE) requirement for the federal fiscal year 2017 grant. This amount includes about \$443 million in expenditures made by other state agencies. When reporting the expenditures of other agencies, the Department must ensure the amounts reported are accurate and complete, or enter into a written agreement with the other agencies specifying that they will do so.

Quarterly financial reports

Federal regulations require the Department to file quarterly financial reports that include details on how both federal and state TANF funds are spent. The Department collects information on a monthly basis and files the federal reports on a quarterly basis. A quarterly report must be filed for each federal grant that is open. At the end of each federal year, the report must include federal and state MOE expenditures.

Annual report

The Department must also file an annual report that contains detailed information on the state's MOE spending for that year. The total MOE expenditures reported on the quarterly financial report at federal fiscal year end must match the expenditures reported on the separate annual report. The Department must keep records that show all costs are allowable and, if from an entity that is not part of the state government, verifiable.

In our last three audits, we reported in findings that the Department did not have adequate internal controls over submitting quarterly and annual reports for the TANF program. The prior year finding numbers are 2017-021, 2016-018 and 2015-021.

Description of Condition

The Department did not have adequate internal controls in place for submitting quarterly and annual reports for the TANF grant.

The Department did not maintain adequate documentation to support its reported MOE expenditures. Specifically, the Department accepted attestations from agencies regarding their MOE expenditures. While the Department provided client data to these agencies for use in identifying potentially eligible expenditures, it did not verify the amounts these agencies provided were accurate and adequately supported.

We also identified errors in the underlying data from other agencies that totaled about \$87,000. These errors were partially identified through statistically valid sampling methods. We estimate an additional \$190,000 was likely reported in error. These errors affected the year-end quarterly report as well as the annual report.

We consider these internal control weaknesses to constitute a significant deficiency.

Cause of Condition

During the audit period, the Department updated its policies and procedures to address the previously identified internal control weaknesses. However, these changes were not implemented by the end of the audit period. Staff who prepared the reports during fiscal year 2018 again relied on communication protocol, data exchange processes and attestations from other state agencies and believed this was sufficient to ensure the reported amounts were correct.

Additionally, management did not adequately monitor to ensure the Department complied with the federal requirements.

Effect of Condition

Not ensuring the accuracy of the required quarterly and annual reports diminishes the federal government's ability to monitor grant funds. Additionally, grant terms allow the grantor to penalize the Department for noncompliance, including suspending or terminating the award.

We were able to examine other supporting data not used by the report preparers to verify that the amounts reported by the Department were materially accurate.

Recommendations

We recommend the Department:

- Establish sufficient written policies and procedures for preparing the reports
- Verify expenditures reported by other state agencies to ensure they are allowable to count as MOE and adequately supported
- Maintain adequate documentation to support reports filed with its federal grantor

Department's Response

The Department does not concur with the overall findings of the State Auditor's Office.

The Department does not concur that it did not have its updated policies and procedures implemented by the end of the audit period. In response to audit findings 2017-018 and 2017-020, the Department continued to host weekly TANF MOE workgroup meetings in which members would review and update policies and procedures to address the previously identified internal control weaknesses. The Department fully implemented these changes March 2018, prior to the end of the audit period.

The Department does not concur with SAOs statement that "Staff who prepared the reports during fiscal year 2018 again relied on communication protocol, data exchange processes and attestations from other state agencies and believed this was sufficient to ensure the reported amounts were correct." In response to audit findings 2017-018 and 2017-020, the Department implemented the use of Memorandums of Understanding (MOUs) at the beginning of each year to ensure the previous year's sources are viable for the current fiscal year. The MOUs give the Department the opportunity to discuss current program operations, allowable activities and expenditures, and develop a projection of expenditures with the partnering source. During presentation of the MOU, the Department also reviews partners' methodologies and record management protocols, and offers training and assistance, if needed. In addition, the Department implemented a quarterly monitoring/reporting schedule for all MOE sources, to ensure reported expenditures are allowable and accurate in a timelier manner. The Department uses the aforementioned processes in addition to attestations to review, to the best of its ability that all expenditures are accurate, verifiable, not used for any other federal matching purpose, and adequately supported. The Department maintains all supporting documentation locally and electronically to support reports filed with its federal grantor.

The Department understands the SAOs perspective on the requirement to verify expenditures reported by other state agencies. The Department will continue to consult with the Office of Financial Management for guidance on establishing internal controls in response to this recommendation. While the Department does not disagree with the SAO that it should verify expenditures to the best of its ability, when unable to do so due to data sensitivity issues, it believes it satisfies the regulations as set forth in Title 45 Section 263.2(1)(e) to ensure expenditures are "verifiable".

The Department does not concur that its management did not adequately monitor to ensure the Department complied with the federal requirements. In response to audit finding 2017-020, the Department implemented quarterly meetings with representatives of the Community Services Division (CSD), the Division of Research and Data Analysis (RDA), and the Division of Finance and Financial Recovery (DFFR) to review the activities and expenditures from all sources. In addition, the

Department hosts weekly TANF MOE workgroup meetings, as outlined in the written policies and procedures collaboratively developed between CSD, RDA, and DFFR.

Auditor's Concluding Remarks

We verified the Department created draft procedures for preparing the quarterly reports, but they did not impact the Department's reporting for federal fiscal year 2017. The procedures, in our judgment, are insufficient to compile the report and do not address how DSHS ensures the MOE expenditures reported by other agencies are allowable to claim.

Additionally, both program staff and RDA staff confirmed that, other than an excel spreadsheet showing totals and a certification, no further supporting documentation was received by the Department to confirm the expenditures that were claimed, how the calculations were performed or if the totals were reviewed prior to being sent to the Department.

The reference to U.S Code of Federal Regulations 45 Section 263.2(1)(e) as justification for only ensuring expenditures are "verifiable", does not apply to expenditures claimed from other state agencies, only other entities such as local governments.

We reaffirm our finding and will review the status of the Department's corrective action during our next audit.

Applicable Laws and Regulations

Title 2 U.S. Code of Federal Regulations Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance) establishes the following applicable requirements:

Section 200.303 Internal controls, states in part:

The non-Federal entity must:

- (a) Establish and maintain effective internal control over the Federal award that provides reasonable assurance that the non-Federal entity is managing the Federal award in compliance with Federal statutes, regulations, and the terms and conditions of the Federal award. These internal controls should be in compliance with guidance in "Standards for Internal Control in the Federal Government" issued by the Comptroller General of the United States or the "Internal Control Integrated Framework", issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).

Section 200.516 Audit findings, states in part:

- (a) *Audit findings reported.* The auditor must report the following as audit findings in a schedule of findings and questioned costs:
 - (1) Significant deficiencies and material weaknesses in internal control over major programs and significant instances of abuse relating to major programs. The auditor's determination of whether a deficiency in internal control is a significant deficiency or material weakness for the purpose of reporting an audit finding is in

relation to a type of compliance requirement for a major program identified in the Compliance Supplement.

The American Institute of Certified Public Accountants defines significant deficiencies and material weaknesses in internal controls over compliance in its *Codification of Statements on Auditing Standards*, section 935, Compliance Audits, as follows:

.11 For purposes of adapting GAAS to a compliance audit, the following terms have the meanings attributed as follows: ...

Deficiency in internal control over compliance. A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance on a timely basis. A deficiency in design exists when (a) a control necessary to meet the control objective is missing, or (b) an existing control is not properly designed so that, even if the control operates as designed, the control objective would not be met. A deficiency in operation exists when a properly designed control does not operate as designed or the person performing the control does not possess the necessary authority or competence to perform the control effectively.

Material weakness in internal control over compliance. A deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a compliance requirement will not be prevented, or detected and corrected, on a timely basis. In this section, a reasonable possibility exists when the likelihood of the event is either reasonably possible or probable as defined as follows:

Reasonably possible. The chance of the future event or events occurring is more than remote but less than likely.

Probable. The future event or events are likely to occur.

Significant deficiency in internal control over compliance. A deficiency, or a combination of deficiencies, in internal control over compliance that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

Title 45, Code of Federal Regulations

Section 265.3 – What reports must the State file on a quarterly basis, states in part:

(a) Quarterly reports

(1) Each State must collect on a monthly basis, and file on a quarterly basis, the data specified in the TANF Data Report and the TANF Financial Report

Section 263.2 – What kinds of State expenditures count toward meeting a State’s basic MOE expenditure requirement, states in part:

(e) Expenditures for benefits or services listed under paragraph (a) of this section may include allowable costs borne by others in the State (e.g., local government), including cash donations from non-Federal third parties (e.g., a non-profit organization) and the value of third party in-kind contributions if:

(1) The expenditure is verifiable and meets all applicable requirements in 45 CFR 75.2 and 75.306;

- (2) There is an agreement between the State and the other party allowing the State to count the expenditure toward its MOE requirement; and,
- (3) The State counts a cash donation only when it is actually spent.

Section 265.9 What information must the State file annually, states in part:

- (a) Each State must file an annual report containing information on the TANF program and the State's MOE program(s) for that year. The report may be filed as:
 - (1) An addendum to the fourth quarter TANF Data Report; or
 - (2) A separate annual report.
- (c) Each State must provide the following information on the State's program(s) for which the State claims MOE expenditures:
 - (1) The name of each program and a description of the major activities provided to eligible families under each such program;
 - (2) Each program's statement of purpose;
 - (3) If applicable, a description of the work activities in each separate State MOE program in which eligible families are participating;
 - (4) For each program, both the total annual State expenditures and the total annual State expenditures claimed as MOE;
 - (5) For each program, the average monthly total number or the total number of eligible families served for which the State claims MOE expenditures as of the end of the fiscal year;
 - (6) The eligibility criteria for the families served under each program/activity;
 - (7) A statement whether the program/activity had been previously authorized and allowable as of August 21, 1996, under section 403 of prior law;
 - (8) The FY 1995 State expenditures for each program/activity not authorized and allowable as of August 21, 1996, under section 403 of prior law (see § 263.5(b) of this chapter); and
 - (9) A certification that those families for which the State is claiming MOE expenditures met the State's criteria for "eligible families."
- (d) If the State has submitted the information required in paragraphs (b) and (c) of this section in the State Plan, it may meet the annual reporting requirements by reference in lieu of re-submission. If the information in the annual report has not changed since the previous annual report, the State may reference this information in lieu of re-submission.

Section 265.10 When is the annual report due?

The annual report required by § 265.9 is due at the same time as the fourth quarter TANF Data Report.

Section 265.4 When are quarterly reports due?

- (a) Each State must file the TANF Data Report and the TANF Financial Report (or, as applicable, the Territorial Financial Report) within 45 days following the end of the quarter or be subject to a penalty.
- (b) Each State that claims MOE expenditures for a separate State program(s) must file the SSP-MOE Data Report within 45 days following the end of the quarter or be subject to a penalty.

- (c) A State that fails to submit the reports within 45 days will be subject to a penalty unless the State files complete and accurate reports before the end of the fiscal quarter that immediately succeeds the quarter for which the reports were required to be submitted.

2018-030

The Department of Social and Health Services did not have adequate internal controls over and did not comply with client eligibility requirements for the Working Connections Child Care program.

Federal Awarding Agency: U.S. Department of Health and Human Services
Pass-Through Entity: None
CFDA Number and Title: 93.558 Temporary Assistance for Needy Families
93.575 Child Care and Development Block Grant
93.596 Child Care Mandatory and Matching Funds of the Child Care and Development Fund

Federal Award Number: 1801WATANF; 1801WATAN3; 1701WATANF;
1701WATAN3G1801WACCDF; G1701WACCDF;
G1601WACCDF;

Applicable Compliance Component: Eligibility
Known Questioned Cost Amount: Temporary Assistance for Needy Families - \$13,717
Child Care and Development Fund - \$24,242

Background

The Department of Children, Youth and Family (DCYF), formerly the Department of Early Learning, administers the federal Child Care and Development grant (CCDF) to help eligible working families pay for childcare. The Department of Social and Health Services (DSHS) determines client eligibility and pays childcare providers under an agreement with DCYF. The Temporary Assistance for Needy Families (TANF) grant funds may be used to pay clients' childcare costs to meet one of the program's primary purposes of helping clients obtain employment. If a client obtains employment and is no longer eligible for the program, TANF funds may still be used to pay childcare costs to help the client maintain employment.

In fiscal year 2017, the Departments paid childcare providers about \$267 million in CCDF and TANF federal grant funds.

Some payments made for childcare are paid for by both the CCDF grant and the TANF grant. While the two federal programs are separate, the requirements and policies in Washington for childcare payments are consolidated under the Working Connections Child Care program.

For a family to be eligible for childcare assistance, state and federal rules require that children:

- Be younger than 13 (with some exceptions);
- Reside with a family whose income does not exceed 200 percent of the federal poverty level;
- Reside with a family whose income does not increase to over 85 percent of state, territorial or tribal median income for a family of the same size; and

- Reside with a parent or parents who work or attend a job-training or education program, or need to be receiving protective services.

State rules describe the information that clients must provide to DSHS to verify their eligibility. DSHS must complete client eligibility determinations within 30 days, or the application process must start over. The information must be accurate, complete, consistent and from a reliable source. This information includes, but is not limited to, employer and hourly wage information or proof of an approved activity under TANF, wage data and family household size and composition.

Once determined to be eligible for the program, a client is eligible for one year unless a change in income causes the client to exceed 85 percent of the state's median income. DSHS requires that clients self-report such income changes. If the client's new income exceeds this cutoff level, DSHS must determine if the client exceeded the threshold temporarily, or should be denied services.

DSHS has access to systems that contain wage and household benefit and composition data for some, but not all, childcare recipients. DSHS uses this information in part to determine program eligibility, benefit level including client co-payment and the amount of childcare the family is eligible to receive. If an ineligible client receives assistance, the payment made to the childcare provider is not allowable by federal regulations.

In the past six single audits for Washington, we reported in findings that DSHS did not have adequate internal controls over the eligibility process for childcare subsidy recipients. The three most recent audits also reported DSHS was materially non-compliant with federal requirements. These were reported as finding numbers 2017-026, 2016-023, 2015-026, 2014-026, 2013-017 and 12-30.

Description of Condition

DSHS did not have adequate internal controls to ensure it correctly determined and adequately documented clients were eligible before paying childcare providers.

Improper eligibility determinations

During the audit period, 46,367 clients were determined to be eligible for childcare. We used a statistical sampling method to randomly select and examine 91 of these determinations. In 30 instances (33 percent), we found DSHS made eligibility determinations improperly, did not obtain required documentation or did not verify information before authorizing services.

Specifically, we found:

- Seventeen cases (19 percent) where benefit levels were improperly calculated.
 - Nine where an inaccurate determination was made even though the client submitted adequate support
 - Five where the case worker did not obtain enough information to make an accurate determination
 - Three where it was determined care was not actually needed

- Thirteen cases (14 percent) that did not meet initial eligibility requirements and benefits were improperly calculated
 - Six where DSHS did not use the data provided, resulting in inaccurate calculations. In two of these cases, the client was not eligible to receive services.
 - Seven cases where there were questions about how many people were living in the home and how much income they made, and DSHS did not request sufficient documentation or perform other follow up actions to verify. In two of these cases, the parent applied and was denied services due to the other adult living in the home not working or because their income was too high. The clients then re-applied, stating that the other adult was no longer in the home, but DSHS did not follow up to verify this information and approved them to receive benefits.

Inadequate supervisory reviews

In most cases, a DSHS caseworker processes client eligibility information and authorizes services without a secondary review or approval. For authorizations requiring more than standard full-time care, DSHS policy requires staff to use a special authorization code. The code does not become active until a supervisor has reviewed and approved the request.

We found two authorizations that were reviewed by a supervisor but were processed improperly. In one instance, the client was over the income limit, which was not identified during review. In the second instance, DSHS had information showing another adult in the home, and further information was not collected to determine if the eligibility determination was proper.

Internal reviews

DSHS performs multiple types of internal audits in relation to the CCDF program. These audits usually have a particular focus and do not address all areas regarding a particular client's eligibility. These audits have found significant noncompliance for many years. During the audit period, DSHS identified about \$11.6 million in overpayments. Last year, these examinations identified about \$23.8 million in overpayments. DSHS classifies the error trends each year and for at least the last four years has identified incorrect income budgeting, incorrect care authorizations and incorrect co-payment determinations as error trends. Despite being aware of these issues, DSHS has not implemented sufficient internal controls to address and correct them.

We consider these internal control deficiencies to be a material weakness for the CCDF program and a significant deficiency for the TANF program.

Cause of Condition

DSHS staff made eligibility determinations without requiring sufficient supporting documentation to ensure the client was eligible, such as three months' of wage information and wage information for a secondary adult in the home. While DSHS has policies and procedures, they are not detailed enough to ensure staff document determinations in a consistent manner. These policies and procedures were also not in line with the CCDF plan approved by the federal grantor. Additionally, management did not ensure staff consistently followed the procedures that were in place.

While DSHS audits of eligibility determinations identify errors after the fact, this has not been effective in preventing clients from being improperly approved.

Effect of Condition and Likely Questioned Costs

Because it does not have adequate internal controls in place, DSHS is at a higher risk of paying providers for childcare services when clients are ineligible.

Of the 30 client eligibility determinations we identified with errors, 23 resulted in \$37,959 of federal overpayments to providers. Of this amount, \$24,242 was paid with CCDF grant funds and \$13,717 was paid with TANF grant funds.

CCDF questioned costs

The following is a breakdown of the \$24,242 in questioned costs paid with CCDF grant funds:

- \$2,151 was paid for care that was not needed due to the parent's schedule.
- \$6,615 was paid for clients whose income exceeded the allowable amount to receive childcare.
- \$4,150 was paid to clients who had an inaccurate co-pay assessed.
- \$11,326 was paid to clients from whom DSHS did not collect the required documentation to determine their eligibility.

TANF questioned costs

The following is a breakdown of the \$13,717 in questioned costs paid with TANF grant funds:

- \$3,031 was paid for care that was not needed due to the parent's schedule.
- \$3,007 was paid for clients whose income exceeded the allowable amount to receive childcare.
- \$1,842 was paid to clients who had an inaccurate co-pay assessed.
- \$5,837 was paid to clients from whom DSHS did not collect the required documentation to determine their eligibility.

Because we used a statistical sampling method to randomly select the payments examined in the audit, we estimate the amount of likely federal improper payments to be \$16,121,480 for the CCDF grant and \$8,300,491 for the TANF grant.

Further, many of the improper payments were partially funded by state dollars. Specifically, we found \$796 of improper CCDF state payments and \$48 in improper TANF state payments, which projects to a likely improper payment amount of \$533,346 for CCDF and \$33,351 for TANF. This amount is not included in the federal questioned costs.

We question costs when we find an agency has not complied with grant regulations or when it does not have adequate documentation to support its expenditures.

Our sampling methodology meets statistical sampling criteria under generally accepted auditing standards in AU-C 530.05. It is important to note that the sampling technique we used is intended to support our audit conclusions by determining if expenditures were in compliance with program requirements in all material respects. Accordingly, we used an acceptance sampling formula designed to provide a high level of assurance, with a 95 percent confidence of whether exceptions exceeded our materiality threshold. This conclusion is reflected in our audit report and finding. However, the likely questioned costs projections are a point estimate and only represent our “best estimate of total questioned costs” as required by 2 CFR 200.516(3).

Recommendations

We recommend DSHS improve its internal controls over determining eligibility to ensure:

- Authorizations for childcare are adequately supported with verified documentation
- Eligibility determinations are reviewed sufficiently to detect improper eligibility determinations
- Employees review client eligibility documents and compare those documents with source data available to DSHS staff
- Income and household composition are adequately supported and accurate

We also recommend DSHS consult with the grantor to discuss whether the questioned costs identified in the audit should be repaid.

Department’s Response

The Department of Social and Health Services (DSHS) appreciates, acknowledges and supports the State Auditor’s Office’s (SAO) mission, which is to hold state and local government accountable for the use of public resources. Further, we particularly appreciate SAO’s work with us over the past year to strengthen the auditing process.

In response to DSHS 2016-028 and 2017-026 CCDF Eligibility Findings, the Department enacted major changes to improve our internal controls over determining eligibility. However, many of these changes were implemented during the SFY 18 audit period, with some changes not implemented until after the end of the SFY 18 audit period. Therefore, in our response to the SFY 17 audit findings, we acknowledged we were likely to see these same findings in the SFY 18 audit period. We have outlined, below, the major changes that resulted in our improved internal controls.

SAO Description of Weakness: *Improper Eligibility Determinations* – *DSHS made improper eligibility determinations, did not obtain required documentation or did not verify information before authorizing services.*

*Of the 30 exceptions cited, the Department **concurs** that we did not comply with eligibility requirements to some degree for 29 exceptions. Within these 29 exceptions, however, our further review indicates that minor procedural errors had no effect on 10 of these exceptions - we accurately determined eligibility resulting in no overpayments to the clients.*

For the 19 exceptions that we agree resulted in a payment error, in 10 of these cases the client was eligible, however, either the copayment or the amount of care authorized was incorrect, resulting in a partial payment error.

The Department will establish overpayments where appropriate and refer it to the Office of Financial Recovery for collection.

*The Department **does not** concur that we did not comply with eligibility requirements for one exception.*

The Department collaborated with the Department of Children, Youth, and Families (DCYF) to update policies and procedures, and develop system enhancements to correct weaknesses and improve internal controls:

- *Effective August 30, 2017, the Department implemented automation enhancements to auto-generate a sixty-day reminder letter requesting income verification of new employment.*
- *Effective March 1, 2018, the Department, in conjunction with DCYF, updated the appropriate WACs, procedures, and trainings to strengthen verification of household composition including mandatory cross-matching with other state systems, and to clarify required documentation regarding new employment wage verification within sixty days of the Department's request.*
 - *This improved the automation enhancement the Department completed on February 21, 2017 to add a flag when the household composition for child care is different than household composition information entered in other state systems.*
- *As of October 1, 2018, new Family, Friend, and Neighbor (FFN) providers are required to receive DCYF's full Portable Background Check (PBC) and be approved by DCYF as a provider. DCYF creates a vendor number once the provider is approved and the provider's eligibility and vendor number is communicated with DSHS. DSHS must have this vendor number and approval to create an authorization. This separation of duties creates stronger internal controls and reduces the possibility of an ineligible provider receiving an authorization for payment.*

SAO Description of Weakness: Inadequate Supervisory Review - *In most cases, a DSHS caseworker processes client eligibility information and authorizes services without a secondary review or approval. For authorizations requiring more than standard full-time care, DSHS policy requires staff to use a special authorization code. The code does not become active until a supervisor has reviewed and approved the request. We found two authorizations that were reviewed by a supervisor but were processed improperly.*

The Department partially concurs with this description. Child care program policy, set by DCYF, only requires supervisor approval when certain criteria is met, for example, when additional days of care that exceeds twenty-three full days or thirty half days. Policy does not require secondary review or approval when determining eligibility, and authorizing benefits and payment. However, the Department continues to employ the following controls to ensure child care subsidy payment authorizations are made correctly:

- *The Department requires a supervisory review of payment requests that exceed certain parameters. The supervisor reviews the need for the additional payment and either approves the payment by submitting the authorization to the DSHS Social Service Payment System (SSPS) or denies the payment if the consumer is not eligible. In July 2017, the Department added a monthly report to check for any situations where it appeared that an authorization may have been approved without the required secondary review. This report has confirmed that most cases are being handled appropriately.*
- *For authorizations with high cost special needs rates, a panel consisting of DSHS and DCYF staff review the request and supporting documentation prior to approval, and then a supervisor reviews the authorization prior to payment.*
- *The Department requires that 100 percent of new employees' work is audited by a lead worker until they achieve proficiency. These reviews may be conducted either pre or post-authorization.*

In addition, the Department implemented the following supplementary supervisory review:

- *In certain circumstances, employees code cases considered at high risk for error using a "9" code which requires a supervisory review prior to authorization. Beginning July 2017 and monthly thereafter, Centralized Auditors review a (new) 9-code avoidance report which identifies cases that are flagged for potentially requiring 9-coded care (supervisory approval). The Centralized Auditor reviews the cases and follows up with the original agent for coaching and corrective action.*
- *In conjunction with DCYF, the Department implemented changes that increase internal controls to prevent potential employee fraud. Beginning in June 2018, the eligibility system automatically flags any case an agent has accessed without prompting by the system. Supervisors or leads then conduct integrity reviews of these cases.*

SAO Description of Weakness: Internal reviews - DSHS performs multiple types of internal audits in relation to the CCDF program. These audits usually have a particular focus and do not address all areas regarding a particular client's eligibility. DSHS classifies the error trends each year and for at least the last four years has identified incorrect income budgeting, incorrect care authorizations and incorrect co-payment determinations as error trends. Despite being aware of these issues, DSHS has not implemented sufficient internal controls to address and correct them.

The Department partially concurs with this description. The Department has made significant improvements to ensure correct eligibility determinations. However, the trends identified above are overly broad and unlikely to change as they are the three largest pivot points in all determinations. We continue to employ the following controls to ensure child care subsidy payment authorizations are made correctly:

- *Audit at least one percent of child care cases monthly. As reported quarterly to DCYF, these audits average about four percent of the overall caseload.*
- *Review payment requests that exceed certain parameters.*
- *Audit 100% pre/post authorization for all new child care eligibility staff until they attain proficiency.*

- *Participate in the Improper Payments Information Act (IPIA) audit required by the Federal Office of Child Care and conducted by the DCYF once every three years. In federal fiscal year 2017, this audit found that less than three percent of the total amount of payments for the sampled cases were made in error.*
- *Review cases, or refer to DCYF for a provider review, where it appears likely that an improper payment may have occurred. Reviews include requesting attendance records to determine whether an overpayment occurred, whether it was a provider or client that was overpaid, the amount of the improper payment and establishing an overpayment if appropriate.*

Beginning in February 2018, the Department implemented a child care Process Review Panel (PRP). Based on the highly-successful and established model that produces an average 95% accuracy rate in federal Supplemental Nutrition Assistance Program (SNAP) eligibility determination, the PRP introduced the same rigor and attention to eligibility determinations for child care subsidies. The Department's Division of Program Integrity Child Care Quality team reviews cases selected based on a statistically valid methodology, verifies case circumstances and arrives at quality control determinations about whether each sampled case has been correctly determined in accordance with state policy and procedure. The Department uses the results of this case-error review system to inform programmatic, process, systems and policy-level continuous improvement prioritization and implementation. The system also identifies cases with a high risk of error and informs decisions about pre-authorization reviews.

In conclusion, the Department acknowledges the State Auditor's findings and appreciates the Auditor's willingness to work with us to strengthen the Working Connections Child Care Program. The Department has greatly improved and will continue to improve internal controls over eligibility determination. The Department's actions in response to the State Auditor's findings have yielded a precipitous decline in overpayments.

Beginning July 1, 2019, the Department will transfer responsibility for administering all aspects of client eligibility determination and child care provider payment under the Child Care Development Fund (CCDF) to DCYF. While the Department continues to play an active role in supporting continuous improvements within the Working Connections Child Care Program, we acknowledge that subsequent changes and enhancements to this program are within the purview of DCYF.

If the grantor contacts the Department regarding questioned costs that should be repaid, the Department will confirm these costs with the Department of Health and Human Services and will take appropriate action.

Auditor's Concluding Remarks

We thank the Department for its cooperation and assistance throughout the audit. We will review the status of the Department's corrective action during our next audit.

Applicable Laws and Regulations

Title 2 U.S. Code of Federal Regulations Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance) establishes the following applicable requirements:

Section 200.53 Improper Payments states:

- (a) *Improper payment* means any payment that should not have been made or that was made in an incorrect amount (including overpayments and underpayments) under statutory, contractual, administrative, or other legally applicable requirements; and
- (b) *Improper payment* includes any payment to an ineligible party, any payment for an ineligible good or service, any duplicate payment, any payment for a good or service not received (except for such payments where authorized by law), any payment that does not account for credit for applicable discounts, and any payment where insufficient or lack of documentation prevents a reviewer from discerning whether a payment was proper.

Section 200.303 Internal controls, states in part:

The non-Federal entity must:

- (a) Establish and maintain effective internal control over the Federal award that provides reasonable assurance that the non-Federal entity is managing the Federal award in compliance with Federal statutes, regulations, and the terms and conditions of the Federal award. These internal controls should be in compliance with guidance in “Standards for Internal Control in the Federal Government” issued by the Comptroller General of the United States or the “Internal Control Integrated Framework”, issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).
- (b) Comply with Federal statutes, regulations, and the terms and conditions of the Federal awards.
- (d) Take prompt action when instances of noncompliance are identified including noncompliance identified in audit findings.

Section 200.403 Factors affecting Allowability of costs.

Except where otherwise authorized by statute, costs must meet the following general criteria in order to be allowable under Federal awards.

- (a) Be necessary and reasonable for the performance of the Federal award and be allocable thereto under these principles.
- (b) Conform to any limitations or exclusions set forth in these principles or in the Federal award as to types or amount of cost items.
- (c) Be consistent with policies and procedures that apply uniformly to both federally-financed and other activities of the non-Federal entity.
- (d) Be accorded consistent treatment. A cost may not be assigned to a Federal award as a direct cost if any other cost incurred for the same purpose in like circumstances has been allocated to the Federal award as an indirect cost.

- (e) Be determined in accordance with generally accepted accounting principles (GAAP), except, for state and local governments and Indian tribes only, as otherwise provided for in this part.
- (f) Not be included as a cost or used to meet cost sharing or matching requirements of any other federally-financed program in either the current or a prior period. See also §200.306 Cost sharing or matching paragraph (b).
- (g) Be adequately documented. See also §§200.300 Statutory and national policy requirements through 200.309 Period of performance of this part.

Section 200.410 Collection of unallowable costs.

Payments made for costs determined to be unallowable by either the Federal awarding agency, cognizant agency for indirect costs, or pass-through entity, either as direct or indirect costs, must be refunded (including interest) to the Federal Government in accordance with instructions from the Federal agency that determined the costs are unallowable unless Federal statute or regulation directs otherwise. See also Subpart D—Post Federal Award Requirements of this part, §§200.300 Statutory and national policy requirements through 200.309 Period of performance.

Section 200.516 Audit findings, states in part:

- (a) *Audit findings reported.* The auditor must report the following as audit findings in a schedule of findings and questioned costs:
 - (1) Significant deficiencies and material weaknesses in internal control over major programs and significant instances of abuse relating to major programs. The auditor's determination of whether a deficiency in internal control is a significant deficiency or material weakness for the purpose of reporting an audit finding is in relation to a type of compliance requirement for a major program identified in the Compliance Supplement.
 - (2) Material noncompliance with the provisions of Federal statutes, regulations, or the terms and conditions of Federal awards related to a major program. The auditor's determination of whether a noncompliance with the provisions of Federal statutes, regulations, or the terms and conditions of Federal awards is material for the purpose of reporting an audit finding is in relation to a type of compliance requirement for a major program identified in the compliance supplement.
 - (3) Known questioned costs that are greater than \$25,000 for a type of compliance requirement for a major program. Known questioned costs are those specifically identified by the auditor. In evaluating the effect of questioned costs on the opinion on compliance, the auditor considers the best estimate of total costs questioned (likely questioned costs), not just the questioned costs specifically identified (known questioned costs). The auditor must also report known questioned costs when likely questioned costs are greater than \$25,000 for a type of compliance requirement for a major program. In reporting questioned costs, the auditor must include information to provide proper perspective for judging the prevalence and consequences of the questioned costs.

The American Institute of Certified Public Accountants defines significant deficiencies and material weaknesses in internal controls over compliance in its *Codification of Statements on Auditing Standards*, section 935, Compliance Audits, as follows:

.11 For purposes of adapting GAAS to a compliance audit, the following terms have the meanings attributed as follows: ...

Deficiency in internal control over compliance. A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance on a timely basis. A deficiency in design exists when (a) a control necessary to meet the control objective is missing, or (b) an existing control is not properly designed so that, even if the control operates as designed, the control objective would not be met. A deficiency in operation exists when a properly designed control does not operate as designed or the person performing the control does not possess the necessary authority or competence to perform the control effectively.

Material weakness in internal control over compliance. A deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a compliance requirement will not be prevented, or detected and corrected, on a timely basis. In this section, a reasonable possibility exists when the likelihood of an event occurring is either reasonably possible or probable as defined as follows:

Reasonably possible. The chance of the future event or events occurring is more than remote but less than likely.

Probable. The future event or events are likely to occur.

Significant deficiency in internal control over compliance. A deficiency, or a combination of deficiencies, in internal control over compliance that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

Material noncompliance. In the absence of a definition of material noncompliance in the governmental audit requirement, a failure to follow compliance requirements or a violation of prohibitions included in the applicable compliance requirements that results in noncompliance that is quantitatively or qualitatively material, either individually or when aggregated with other noncompliance, to the affected government program.

45 CFR 98.20 A child's eligibility for child care services, states:

- (a) To be eligible for services under §98.50, a child shall, at the time of eligibility determination or redetermination:
 - (1) (i) Be under 13 years of age; or,
 - (ii) At the option of the Lead Agency, be under age 19 and physically or mentally incapable of caring for himself or herself, or under court supervision;
- (2) (i) Reside with a family whose income does not exceed 85 percent of the State's median income (SMI), which must be based on the most recent SMI data that is published by the Bureau of the Census, for a family of the same size; and

- (ii) Whose family assets do not exceed \$1,000,000 (as certified by such family member); and
- (3) (i) Reside with a parent or parents who are working or attending a job training or educational program; or
 - (ii) Receive, or need to receive, protective services, which may include specific populations of vulnerable children as identified by the Lead Agency, and reside with a parent or parents other than the parent(s) described in paragraph (a)(3)(i) of this section.
 - (A) At grantee option, the requirements in paragraph (a)(2) of this section may be waived for families eligible for child care pursuant to this paragraph, if determined to be necessary on a case-by-case basis.
 - (B) At grantee option, the waiver provisions in paragraph (a)(3)(ii)(A) of this section apply to children in foster care when defined in the Plan, pursuant to §98.16(g)(7).
- (b) A grantee or other administering agency may establish eligibility conditions or priority rules in addition to those specified in this section and §98.46, which shall be described in the Plan pursuant to §98.16(i)(5), so long as they do not:
 - (1) Discriminate against children on the basis of race, national origin, ethnic background, sex, religious affiliation, or disability;
 - (2) Limit parental rights provided under subpart D of this part;
 - (3) Violate the provisions of this section, §98.46, or the Plan. In particular, such conditions or priority rules may not be based on a parent's preference for a category of care or type of provider. In addition, such additional conditions or rules may not be based on a parent's choice of a child care certificate; or
 - (4) Impact eligibility other than at the time of eligibility determination or redetermination.
- (c) For purposes of implementing the citizenship eligibility verification requirements mandated by title IV of the Personal Responsibility and Work Opportunity Reconciliation Act, 8 U.S.C. 1601 et seq., only the citizenship and immigration status of the child, who is the primary beneficiary of the CCDF benefit, is relevant. Therefore, a Lead Agency or other administering agency may not condition a child's eligibility for services under §98.50 based upon the citizenship or immigration status of their parent or the provision of any information about the citizenship or immigration status of their parent.

WAC 170-290-0005 Eligibility, states:

- (1) At application and reapplication, to be eligible for WCCC, the applicant or reapplicant must:
 - (a) Have parental control of one or more eligible children;
 - (b) Live in the state of Washington;
 - (c) Be the child's:
 - (i) Parent, either biological or adopted;
 - (ii) Stepparent;
 - (iii) Legal guardian verified by a legal or court document;
 - (iv) Adult sibling or step-sibling;
 - (v) Nephew or niece;

- (vi) Aunt;
- (vii) Uncle;
- (viii) Grandparent;
- (ix) Any of the relatives in (c)(vi), (vii), or (viii) of this subsection with the prefix "great," such as great-aunt; or
- (x) An approved in loco parentis custodian responsible for exercising day-to-day care and control of the child and who is not related to the child as described above;
- (d) Participate in an approved activity under WAC 170-290-0040, 170-290-0045, 170-290-0050, or have been approved per WAC 170-290-0055;
- (e) Comply with any special circumstances that might affect WCCC eligibility under WAC 170-290-0020;
- (f) Have countable income at or below two hundred per- cent of the federal poverty guidelines (FPG) and have resources under one million dollars per WAC 170-290-0022;
- (g) The consumer's eligibility shall end if the consumer's countable income is greater than eighty-five percent of the state median income or if resources exceed one million dollars;
- (h) Complete the WCCC application and DSHS verification process provided in WAC 170-290-0012 regardless of other program benefits or services received;
- (i) Effective March 1, 2018, certify under penalty of per- jury, the applicant's or reapplicant's status as:
 - (i) Married;
 - (ii) Unmarried and living with the parent of any child in the household; or
 - (iii) Single parent not living with the parent of any child in the household.
- (j) Meet eligibility requirements for WCCC described in Part II of this chapter.
- (2) Children. To be eligible for WCCC, the child must:
 - (a) Belong to one of the following groups as defined in WAC 388-424-0001:
 - (i) A U.S. citizen;
 - (ii) A U.S. national;
 - (iii) A qualified alien; or
 - (iv) A nonqualified alien who meets the Washington state residency requirements as listed in WAC 388-468-0005;
 - (b) Live in Washington state, and be:
 - (i) Less than thirteen years of age; or
 - (ii) Less than nineteen years of age, and:
 - (A) Have a verified special need, according WAC 170-290-0220; or
 - (B) Be under court supervision.

WAC 170-290-0012 Verifying consumers' information, states:

- (1) When a consumer initially applies or reapplies for benefits, DSHS requires the consumer to provide verification of child care subsidy eligibility if the department is unable to verify through agency records or systems.
- (2) During the consumer's eligibility period, DSHS will request verification for changes that may affect the consumer's benefit amount or eligibility when the department is unable to verify through agency records or systems if:

- (a) The consumer reports a change;
 - (b) DSHS discovers the consumer's circumstances have changed; or
 - (c) The information DSHS has is questionable or outdated.
- (3) DSHS notifies the consumer when verification is required.
- (4) DSHS may accept verification to support the consumer's statement of circumstances. The verification the consumer gives DSHS must:
- (a) Clearly relate to what the consumer is trying to provide;
 - (b) Be from a reliable source; and
 - (c) Be accurate, complete, and consistent.
- (5) When the consumer gives DSHS questionable verification DSHS will:
- (a) Ask the consumer to provide DSHS with more verification or provide a collateral contact (a "collateral contact" is a statement from someone outside of the consumer's residence that knows the consumer's situation); or
 - (b) Send an investigator from the DSHS office of fraud and accountability (OFA) to make an unannounced visit to the consumer's home to verify the consumer's circumstances. Consumer's rights are found in WAC 170-290-0025.
- (6) At the time of application, reapplication, or when changes are reported, DSHS will verify the following:
- (a) The consumer's Washington residency;
 - (b) That the consumer has parental control of an eligible child per WAC 170-290-0005;
 - (c) The consumer's household composition:
 - (i) DSHS will compare the consumer's statement of household composition against records for that consumer under TANF, food assistance, medical assistance, and child support services;
 - (ii) If the consumer's statement of household composition is questionable when compared against records for that consumer under TANF, food assistance, medical assistance, and child support services, DSHS may take the action described in subsection (5) of this section; and
 - (iii) Effective March 1, 2018, if the consumer is the only parent named on the benefits application and DSHS is unable to verify household composition in agency records under TANF, food assistance, medical assistance, or child support services, then the consumer must:
 - (A) Provide the name and address of the other parent, or indicate, under penalty of perjury, that the other parent's identity and address are unknown to the applicant or that providing this information will likely result in serious physical or emotional harm to the consumer or anyone residing with the consumer; and
 - (B) Indicate under penalty of perjury whether the parent is present or absent in the household;
 - (d) Whether the consumer is participating in an approved activity, including the consumer's income and schedule from the approved activity;
 - (e) Whether the consumer complies with applicable eligibility rules in WAC 170-290-0020;
 - (f) Other income and countable resources under WAC 170-290-0005;
 - (g) If any other parent, as determined in WAC 170-290-0015, is in the household, the same information in (a) through (g) of this subsection is verified for that parent; and
 - (h) The citizenship or alien status of a child receiving child care subsidies.

- (7) If DSHS requires verification from a consumer that costs money, DSHS must pay for the consumer's reasonable costs.
- (8) DSHS does not pay for a self-employed consumer's state business registration or license, which is a cost of doing business.
- (9) If a consumer does not provide all of the verification requested within thirty days from the application date, DSHS will determine the consumer's eligibility based on the information already available to DSHS. DSHS shall deny the application or reapplication if the available information does not confirm eligibility.

2018-031 The Department of Social and Health Services improperly charged payroll costs to the Child Support Enforcement Grant.

Federal Awarding Agency: U.S. Department of Health and Human Services
Pass-Through Entity: None
CFDA Number and Title: 93.563 Child Support Enforcement
Federal Award Number: 1704WACEST, 1704WACSES, 1804WACEST, 1804WACSES
Applicable Compliance Component: Activities Allowed or Unallowed and Allowable Costs/Cost Principles
Known Questioned Cost Amount: \$29,733

Background

The Department of Social and Health Services, Division of Child Support, (Department) administers the Child Support Enforcement grant. The grant provides financial support to families by locating noncustodial parents, establishing and enforcing child support orders, establishing and enforcing medical insurance coverage, establishing paternity, and collecting and paying child and spousal support payments.

The Department operates under federal regulations as well as a state plan that is approved every year. The Department is allowed to spend federal grant money on administrative costs to run the program. Staff bill 100 percent of their time to the Child Support Enforcement grant, and the Department uses a monthly certification process to ensure time is billed accurately. Any employee who did not work 100 percent of their time on the grant must submit a timesheet. At the end of each month, the Department creates journal vouchers (JVs) to allocate the payroll costs from the Child Support Enforcement grant to other activities associated with work by these employees.

In fiscal year 2018, the Department spent over \$112 million in federal funds on the program; about \$62 million of this amount was for salaries and benefits.

In the prior audit, we reported the Department did not properly allocate payroll costs to the Child Support Enforcement Grant. The prior finding number was 2017-023.

Description of Condition

We examined the payroll costs charged for five months of the fiscal year and found the Department improperly charged \$29,733 in payroll costs to the Child Support Enforcement Grant.

Cause of Condition

The Department said some timesheets were not processed, the template used to calculate transfers had formula errors and the JV for one monthly transfer was not processed.

Effect of Condition and Questioned Costs

We found \$29,733 in direct payroll and benefits charged to the Child Support Enforcement grant that should have been allocated to other grants. We used a non-statistical sampling approach to select the transactions we selected for audit and estimate the total amount of likely improper payments to be \$71,359. Because the expenditures for this program are funded with both federal and state dollars, we also identified \$15,317 in improper state payments with a likely improper payment amount of \$36,761.

We question costs when we find an agency has not complied with grant regulations or when it does not have adequate documentation to support its expenditures.

Recommendation(s)

We recommend the Department:

- Ensure all required timesheets are processed
- Ensure formulas used to perform calculations are correct
- Ensure all JVs are processed
- Consult with the grantor to discuss whether the questioned costs identified in the audit should be repaid.

Department's Response

At the time of the audit, the Department concurred with the State Auditor's Office's (SAO) findings. However, after further research of SAOs testing, the Department revised our stance to partially concur with this finding.

The Department concurs the template used to calculate transfers had formula errors and the JV for one monthly transfer was not processed.

Prior to the audit finding, in August 2018, the Department created a new journal voucher (JV) template with correct formulas to perform calculations, and added a supervisory review prior to processing JVs. In addition, the Department changed the process of separating the JVs by funding source to reduce the complexity and volume of JVs.

The Department will also:

- *Correct accounting records to charge the appropriate costs to the Child Support Enforcement grant (returning funds to the grant).*
- *Review current procedures for processing JVs and strengthen appropriately to ensure all JVs going forward are processed*

The Department will ensure the aforementioned corrective actions are implemented effectively and in a timely manner.

The Department does not concur that some timesheets were not processed. The timesheets in question are for employees whose time is spent processing negotiables for another Administration. For this

work, the Department bills (no JV) the other Administration for the work done and brings the receipts in as a reduction to expenditures for Title IV-D.

The Department also does not concur with SAOs total questioned costs of \$29,733. During the state fiscal year (SFY) 2018 Statewide Single Audit (SWSA), the Department was reviewing SAOs testing for audit finding 2017-023 as part of the National External Audit Review (NEAR) process to close the 2017-023 finding with the cognizant federal agency. During the NEAR process the Department discovered the SAO made calculation errors in their testing. Due to this discovery and the requirement to ensure the Department only returns the appropriate funds, the Department started reviewing SAOs SFY 2018 SWSA testing.

The Department's review of audit finding 2018-001 began in November 2018 once the Department discovered the miscalculations that incorrectly resulted in audit finding 2017-023.

In reviewing the SAOs testing for audit 2018-001, the Department found:

- *\$18,909 of the questioned costs was incorrectly included for one employee (covering a three month period) whom is coded to state only.*
- *\$1,817 of the questioned costs was incorrectly included for employees whose time is spent processing negotiables for another Administration, and for work performed on another agencies federal grant. In both of these instances, the Department bills for the work done and brings the receipts in as a reduction to expenditures for Title IV-D.*
- *\$1,128 of the questioned costs was incorrectly included for a JV to transfer costs of an employee that was not included in the sample.*
- *\$926 of the questioned costs was incorrectly included for an employee coded to another grant.*
- *\$677 of the questioned costs was incorrectly included for a journal voucher transferring out costs that were not included in the calculations.*
- *\$792 of the questioned costs was incorrectly included due to miscellaneous errors and rounding.*

Of the \$29,733 questioned costs, the Department determined \$24,250 was due to the aforementioned SAO miscalculations. Therefore, the Department calculates the actual questioned costs as \$5,484.

The Department completed their review and presented their results to the SAO in early February prior to the Statewide Single Audit report being published. However, SAO took the stance not to revise the finding because the Department initially agreed with the exceptions, initially did not have any technical comments, and then initially (based on information the Department trusted as being accurate) concurred with the finding at the time of the audit (which was prior to the Department's discovery of SAOs miscalculations).

If the grantor contacts the Department regarding questioned costs that should be repaid, the Department will confirm these costs with the Department of Health and Human Services and will take appropriate action.

Auditor's Concluding Remarks

Before initially sending this finding to the Department on October 2, 2018, we met with program staff and thoroughly discussed each of the identified exceptions. In every case, Department staff fully agreed with our results. When providing its original, formal response to the finding, the Department again stated that it had reviewed all of the associated questioned costs and concurred, even asking for an extension to give them sufficient time for review, which we granted.

Almost four months later, the Department provided additional information and indicated it no longer agreed with our conclusions. We performed a cursory review to see if further work was required. In our judgment, most of the information the Department asserted was not accurate.

We reaffirm our finding and will review the status of the Department's corrective action during our next audit.

Applicable Laws and Regulations

Title 2 U.S. Code of Federal Regulations Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance) establishes the following applicable requirements:

Section 200.53 Improper Payments states:

- (a) *Improper payment* means any payment that should not have been made or that was made in an incorrect amount (including overpayments and underpayments) under statutory, contractual, administrative, or other legally applicable requirements; and
- (b) *Improper payment* includes any payment to an ineligible party, any payment for an ineligible good or service, any duplicate payment, any payment for a good or service not received (except for such payments where authorized by law), any payment that does not account for credit for applicable discounts, and any payment where insufficient or lack of documentation prevents a reviewer from discerning whether a payment was proper.

Section 200.403 Factors affecting Allowability of costs.

Except where otherwise authorized by statute, costs must meet the following general criteria in order to be allowable under Federal awards.

- (a) Be necessary and reasonable for the performance of the Federal award and be allocable thereto under these principles.
- (b) Conform to any limitations or exclusions set forth in these principles or in the Federal award as to types or amount of cost items.
- (c) Be consistent with policies and procedures that apply uniformly to both federally-financed and other activities of the non-Federal entity.
- (d) Be accorded consistent treatment. A cost may not be assigned to a Federal award as a direct cost if any other cost incurred for the same purpose in like circumstances has been allocated to the Federal award as an indirect cost.

- (e) Be determined in accordance with generally accepted accounting principles (GAAP), except, for state and local governments and Indian tribes only, as otherwise provided for in this part.
- (f) Not be included as a cost or used to meet cost sharing or matching requirements of any other federally-financed program in either the current or a prior period. See also §200.306 Cost sharing or matching paragraph (b).
- (g) Be adequately documented. See also §§200.300 Statutory and national policy requirements through 200.309 Period of performance of this part.

Section 200.410 Collection of unallowable costs.

Payments made for costs determined to be unallowable by either the Federal awarding agency, cognizant agency for indirect costs, or pass-through entity, either as direct or indirect costs, must be refunded (including interest) to the Federal Government in accordance with instructions from the Federal agency that determined the costs are unallowable unless Federal statute or regulation directs otherwise. See also Subpart D—Post Federal Award Requirements of this part, §§200.300 Statutory and national policy requirements through 200.309 Period of performance.

Section 200.516 Audit findings, states in part:

- (a) *Audit findings reported.* The auditor must report the following as audit findings in a schedule of findings and questioned costs:
 - (3) Known questioned costs that are greater than \$25,000 for a type of compliance requirement for a major program. Known questioned costs are those specifically identified by the auditor. In evaluating the effect of questioned costs on the opinion on compliance, the auditor considers the best estimate of total costs questioned (likely questioned costs), not just the questioned costs specifically identified (known questioned costs). The auditor must also report known questioned costs when likely questioned costs are greater than \$25,000 for a type of compliance requirement for a major program. In reporting questioned costs, the auditor must include information to provide proper perspective for judging the prevalence and consequences of the questioned costs.

Section 200.430 Compensation—personal services, states in part:

- (a) General. Compensation for personal services includes all remuneration, paid currently or accrued, for services of employees rendered during the period of performance under the Federal award, including but not necessarily limited to wages and salaries. Compensation for personal services may also include fringe benefits which are addressed in § 200.431 Compensation—fringe benefits. Costs of compensation are allowable to the extent that they satisfy the specific requirements of this part, and that the total compensation for individual employees:

- (1) Is reasonable for the services rendered and conforms to the established written policy of the non-Federal entity consistently applied to both Federal and non-Federal activities;
 - (3) Is determined and supported as provided in paragraph (i) of this section, Standards for Documentation of Personnel Expenses, when applicable.
- (i) Allowable activities. Charges to Federal awards may include reasonable amounts for activities contributing and directly related to work under an agreement, such as delivering special lectures about specific aspects of the ongoing activity, writing reports and articles, developing and maintaining protocols (human, animals, etc.), managing substances/chemicals, managing and securing project-specific data, coordinating research subjects, participating in appropriate seminars, consulting with colleagues and graduate students, and attending meetings and conferences.

2018-032

The Department of Commerce did not have adequate internal controls over and did not comply with requirements to monitor subrecipients of the Low-Income Home Energy Assistance program.

Federal Awarding Agency: U. S. Department of Health and Human Services
Pass-Through Entity: None
CFDA Number and Title: 93.568 Low-Income Home Energy Assistance
Federal Award Number: G-18B1WALIEA, G-17B1WALIEA, G-1701WALIE4, G-16B1WALIEA, G-1601WALIE4
Applicable Compliance Component: Subrecipient Monitoring
Known Questioned Cost Amount: None

Background

The Department of Commerce administers the Low-Income Home Energy Assistance program, which provides assistance to low income households to meet their home energy needs. Community-based organizations receive subawards from the Department to provide this assistance. The organizations perform program eligibility determinations and award grants to eligible households. In fiscal year 2018, the Department spent over \$57 million in federal program funds, almost \$51 million of which was paid to subrecipients.

The Department performs on-site monitoring of subrecipients every three years and performs desk monitoring during the two intervening years. The on-site monitoring and desk monitoring include the review of a selection of eligibility determinations and three individual expenditures paid by the subrecipient with federal funds.

Description of Condition

We found the Department did not have adequate internal controls to ensure subrecipients properly spent the federal funds they received. The monitoring the Department performed was insufficient to ensure it could reasonably detect unallowable or unsupported costs by the community-based organizations. The Department reviewed the documentation for three expenditures at each of the community-based organizations during on-site monitoring and desk monitoring.

We reviewed supporting documentation of five of the 10 on-site monitoring visits and five of the 16 desk reviews the Department performed during the audit period to identify the percentage of federal funds the subrecipient received that were reviewed by the Department. We found the Department reviewed:

- Less than 1 percent of the federal funds in two reviews.
- Less than 2 percent of the federal funds in another three reviews.
- Less than 5 percent of the federal funds in another two reviews.
- Five percent, 12 percent and 16 percent of the federal funds in the other three reviews.

Of the over \$17.7 million spent by these 10 subrecipients, the Department reviewed less than \$550,000 (3 percent).

We consider this internal control deficiency to be a material weakness. This condition was not reported in the prior audit.

Cause of Condition

The Department believed that its monitoring practices were sufficient to detect unallowable or unsupported costs by the local community based organizations. The Department had previously performed more in-depth fiscal monitoring, but discontinued that process prior to the audit period.

Effect of Condition

When sufficient monitoring is not conducted, the likelihood increases that the Department would not detect unallowable or unsupported costs at the community-based organizations.

Recommendation

We recommend the Department strengthen its internal controls regarding how it monitors the activities of subrecipients to ensure subawarded federal funds are used for authorized purposes.

Department's Response

The Department concurs with the audit recommendations to strengthen internal controls regarding monitoring subrecipient activities to ensure the authorized use of subawarded federal funds. Our efforts to enhance detection of unallowable or unsupported costs by the local community based organizations will center on staff training, leveraging department resources to increase coverage, and a data driven approach to fiscal administrative monitoring.

Action Steps:

- *Increase number of reviewed transactions during onsite and desk monitoring. The monitoring team will select the fiscal transactions for review based on the highest three months of spending during the current program year. Staff will select the general ledger and back up documents for every transaction during those months to verify allowed costs. By January 31, 2019, program staff will review and update the LIHEAP monitoring plan to reflect the suggested enhancements to onsite and desk monitoring.*
- *Coordinate with Weatherization to increase fiscal administrative coverage for LIHEAP funds. Weatherization utilizes LIHEAP funding as a portion of their grants to sub-recipients. LIHEAP staff will also attend trainings hosted by Weatherization on fiscal administrative monitoring. By March 29, 2019, the LIHEAP program will coordinate efforts around leveraging fiscal administrative functions of Weatherization monitoring.*
- *Require submission of fiscal back up documentation for invoices during the program year. The LIHEAP team will analyze spending for each local community based organization in the network in order to determine spending trends during the heating season of a five-year period. Based on that analysis, we will identify the highest three months of spending, and will require each local community based organization to submit backup documentation for each*

expense incurred to monitor for allowed costs during the months we have identified. By March 29, 2019, the LIHEAP program will research spending trends and implement required submission of backup documentation for invoices for every sub-recipient.

These three areas of enhancement will increase the likelihood that the department will detect unallowable or unsupported costs at the subrecipient level.

Auditor's Concluding Remarks

We thank the Department for its cooperation and assistance throughout the audit. We will review the status of the Department's corrective action during our next audit.

Applicable Laws and Regulations

Title 2 U.S. Code of Federal Regulations Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance) establishes the following applicable requirements:

Section 200.303 Internal controls, states in part:

The non-Federal entity must:

- (a) Establish and maintain effective internal control over the Federal award that provides reasonable assurance that the non-Federal entity is managing the Federal award in compliance with Federal statutes, regulations, and the terms and conditions of the Federal award. These internal controls should be in compliance with guidance in "Standards for Internal Control in the Federal Government" issued by the Comptroller General of the United States or the "Internal Control Integrated Framework", issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).
- (b) Comply with Federal statutes, regulations, and the terms and conditions of the Federal awards.
- (d) Take prompt action when instances of noncompliance are identified including noncompliance identified in audit findings.

Section 200.331 Requirements for pass-through entities, states in part:

All pass-through entities must:

- (d) Monitor the activities of the subrecipient as necessary to ensure that the subaward is used for authorized purposes, in compliance with Federal statutes, regulations, and the terms and conditions of the subaward; and that subaward performance goals are achieved. Pass-through entity monitoring of the subrecipient must include:
 - (1) Reviewing financial and performance reports required by the pass-through entity.
 - (2) Following-up and ensuring that the subrecipient takes timely and appropriate action on all deficiencies pertaining to the Federal award provided to the subrecipient from the pass-through entity detected through audits, on-site reviews, and other means.

- (3) Issuing a management decision for audit findings pertaining to the Federal award provided to the subrecipient from the pass-through entity as required by §200.521 Management decision.
- (e) Depending upon the pass-through entity's assessment of risk posed by the subrecipient (as described in paragraph (b) of this section), the following monitoring tools may be useful for the pass-through entity to ensure proper accountability and compliance with program requirements and achievement of performance goals:
 - (1) Providing subrecipients with training and technical assistance on program-related matters; and
 - (2) Performing on-site reviews of the subrecipient's program operations;
 - (3) Arranging for agreed-upon-procedures engagements as described in §200.425 Audit services.

Section 200.516 Audit findings, states in part:

- (a) *Audit findings reported.* The auditor must report the following as audit findings in a schedule of findings and questioned costs:
 - (1) Significant deficiencies and material weaknesses in internal control over major programs and significant instances of abuse relating to major programs. The auditor's determination of whether a deficiency in internal control is a significant deficiency or material weakness for the purpose of reporting an audit finding is in relation to a type of compliance requirement for a major program identified in the Compliance Supplement.
 - (2) Material noncompliance with the provisions of Federal statutes, regulations, or the terms and conditions of Federal awards related to a major program. The auditor's determination of whether a noncompliance with the provisions of Federal statutes, regulations, or the terms and conditions of Federal awards is material for the purpose of reporting an audit finding is in relation to a type of compliance requirement for a major program identified in the compliance supplement.

The American Institute of Certified Public Accountants defines significant deficiencies and material weaknesses in internal controls over compliance in its *Codification of Statements on Auditing Standards*, section 935, Compliance Audits, as follows:

.11 For purposes of adapting GAAS to a compliance audit, the following terms have the meanings attributed as follows: ...

Deficiency in internal control over compliance. A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance on a timely basis. A deficiency in design exists when (a) a control necessary to meet the control objective is missing, or (b) an existing control is not properly designed so that, even if the control operates as designed, the control objective would not be met. A deficiency in operation exists when a properly designed

control does not operate as designed or the person performing the control does not possess the necessary authority or competence to perform the control effectively.

Material weakness in internal control over compliance. A deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a compliance requirement will not be prevented, or detected and corrected, on a timely basis. In this section, a reasonable possibility exists when the likelihood of an event occurring is either reasonably possible or probable as defined as follows:

Reasonably possible. The chance of the future event or events occurring is more than remote but less than likely.

Probable. The future event or events are likely to occur.

Significant deficiency in internal control over compliance. A deficiency, or a combination of deficiencies, in internal control over compliance that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

Material noncompliance. In the absence of a definition of material noncompliance in the governmental audit requirement, a failure to follow compliance requirements or a violation of prohibitions included in the applicable compliance requirements that results in noncompliance that is quantitatively or qualitatively material, either individually or when aggregated with other noncompliance, to the affected government program.

2018-033

The Department of Children, Youth, and Families did not have adequate internal controls to ensure payroll charges to the Child Care and Development Fund program were allowable and properly supported.

Federal Awarding Agency: U.S. Department of Health and Human Services
Pass-Through Entity: None
CFDA Number and Title: 93.575 Child Care and Development Block Grant
93.596 Child Care Mandatory and Matching Funds of the Child Care and Development Fund
Federal Award Number: G1801WACCDF; G1701WACCDF; G1601WACCDF
Applicable Compliance Component: Activities Allowed or Unallowed and Allowable Costs/Cost Principles
Known Questioned Cost Amount: \$9,544,526

Background

The Department of Children, Youth, and Families (formerly the Department of Early Learning) administers the federal Child Care and Development Fund (CCDF) grant to help eligible working families pay for childcare.

The Department may use grant funds only for costs that are allowable and related to the grant's purpose. According to Department policy, employees whose positions are funded by a single federal award or a single cost activity must certify twice a year using a semi-annual certification they did not perform any other duties. The certification must be approved by the employee's supervisor who has firsthand knowledge of the activities the employee performed in the prior six-month period. In addition, for employees who work on additional cost activities other than the grant program, they must complete a timesheet twice a month.

In fiscal year 2018, the Department spent almost \$250 million in federal funds on the CCDF program. About \$19 million of that total was for payroll expenses of employees who worked on the program.

Description of Condition

The Department did not have adequate internal controls to ensure payroll charges to the CCDF program were allowable and properly supported.

The Department did not complete the semi-annual certifications on time for the second half of fiscal year 2018 (January 1 to June 30, 2018). These certifications covered 234 employees. The Department's policy states that by July 16, an email notification will be sent to employees who need to submit the semi-annual certifications, and the forms must be completed and reviewed within five business days. They second half of the semi-annual certifications were eventually completed, but more than two months after the Department's due date.

In addition, we identified three instances for the first half of the fiscal year (July 1 to December 31, 2017), when semi-annual certifications or timesheets were not completed for employees to allocate their time. We also found two employees for the second half of the year should have completed timesheets to allocate their time for all or part of the period, but did not.

We consider these internal control deficiencies to be a significant deficiency.

This condition was not reported in the prior audit.

Cause of Condition

The Department had policies in place to ensure compliance, but they were not followed. The semi-annual certifications were not emailed to staff for the period in question, and the supervisors did not ensure the certifications were completed within the designated timeframe as required by Department policy. Additionally, management did not provide sufficient oversight to ensure timely compliance with the requirement.

During the period in question, the Department, as directed by the state legislature, was in the process of closing the Department of Early Learning and creating a new state agency that also merged another state agency. Due to the lack of availability of resources, management considered other areas to be of higher priority for responsible staff with the July 1, 2018 merger deadline. This led to the semi-annual certifications not being completed by the deadline as set in Department policy.

Effect of Condition and Questioned Costs

The Department charged \$9,544,526 in direct payroll and benefits to the CCDF program that were not adequately supported. We are questioning these costs, which consist of:

- \$9,398,547 for the 234 employees who did not complete semi-annual certifications for the second half of the fiscal year
- \$64,630 for the three employees who did not complete the required documentation to support their salary for the first half of the fiscal year
- \$81,349 for the two employees who should have completed time sheets for the second half of the fiscal year

We question costs when we find an agency has not complied with grant requirements or when it does not have adequate documentation to support its expenditures.

Recommendations

We recommend the Department:

- Follow its own policy to ensure payroll costs charged to a federal grant are supported by required documentation
- Consult with the grantor to discuss whether the questioned costs identified in the audit should be repaid

Department's Response

The Department partially concurs with the exceptions that were identified by the State Auditor's Office around the internal controls for payroll charges to the CCDF grant. While the Department concedes that semi-annual certifications, documentation, and timesheets were not completed as described above, we maintain that the cause of the issue was an isolated, exceptional circumstance that no longer presents an internal control issue going forward. Further, we have since completed the semi-annual certifications described above and addressed staff with missing timesheets. In addition, 167 (representing \$6.9 million of the questioned costs) of the employees referenced are licensing or program staff who are 100% eligible for payroll charges to the CCDF grant and who do not perform duties other than those that are approved activities related only to the CCDF program.

As stated in the Cause of Condition, the Department of Early Learning (DEL) was part of the transition to the new state agency, the Department of Children, Youth, and Families (DCYF). The two payroll staff that were responsible for completing the DEL semi-annual certifications were also responsible for onboarding and processing payroll for 3,306 employees during the same time-period. Due to the lack of available resources, DCYF chose to focus staff time on processing the new agency payroll and benefits payments.

The Department maintains that the questioned costs of \$9,398,547 for the 234 employees referenced by SAO was a timing issue and the Department is in compliance with Federal CFR requirements. Once all onboarding tasks were stabilized, the payroll staff completed the semi-annual certifications for the former DEL. Prior to the transition, the payroll certifications were completed by the Department established deadlines and when division managers changed positions or left the agency.

As to the Auditor's specific findings regarding lack of timesheets, DCYF concurs and offers the following additional details:

- *DCYF made retroactive adjustments to employee payroll coding resulting in multiple cost activities being charged. DCYF will implement preventative internal controls over allowable retroactive adjustments to ensure payroll charges are properly documented.*
- *DCYF will continue to review position action requests (PARs) and monthly payroll reports to ensure timesheets are being completed by employees charging to multiple cost activities.*

Auditor's Concluding Remarks

We thank the Department for its cooperation and assistance throughout the audit. We will review the status of the Department's corrective action during our next audit.

Applicable Laws and Regulations

Title 2 U.S. Code of Federal Regulations Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance) establishes the following applicable requirements:

Section 200.53 Improper Payments states:

- (a) *Improper payment* means any payment that should not have been made or that was made in an incorrect amount (including overpayments and underpayments) under statutory, contractual, administrative, or other legally applicable requirements; and
- (b) *Improper payment* includes any payment to an ineligible party, any payment for an ineligible good or service, any duplicate payment, any payment for a good or service not received (except for such payments where authorized by law), any payment that does not account for credit for applicable discounts, and any payment where insufficient or lack of documentation prevents a reviewer from discerning whether a payment was proper.

Section 200.303 Internal controls, states in part:

The non-Federal entity must:

- (a) Establish and maintain effective internal control over the Federal award that provides reasonable assurance that the non-Federal entity is managing the Federal award in compliance with Federal statutes, regulations, and the terms and conditions of the Federal award. These internal controls should be in compliance with guidance in “Standards for Internal Control in the Federal Government” issued by the Comptroller General of the United States or the “Internal Control Integrated Framework”, issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).
- (d) Take prompt action when instances of noncompliance are identified including noncompliance identified in audit findings.

Section 200.403 Factors affecting Allowability of costs.

Except where otherwise authorized by statute, costs must meet the following general criteria in order to be allowable under Federal awards.

- (a) Be necessary and reasonable for the performance of the Federal award and be allocable thereto under these principles.
- (b) Conform to any limitations or exclusions set forth in these principles or in the Federal award as to types or amount of cost items.
- (c) Be consistent with policies and procedures that apply uniformly to both federally-financed and other activities of the non-Federal entity.
- (d) Be accorded consistent treatment. A cost may not be assigned to a Federal award as a direct cost if any other cost incurred for the same purpose in like circumstances has been allocated to the Federal award as an indirect cost.
- (e) Be determined in accordance with generally accepted accounting principles (GAAP), except, for state and local governments and Indian tribes only, as otherwise provided for in this part.
- (f) Not be included as a cost or used to meet cost sharing or matching requirements of any other federally-financed program in either the current or a prior period. See also §200.306 Cost sharing or matching paragraph (b).
- (g) Be adequately documented. See also §§200.300 Statutory and national policy requirements through 200.309 Period of performance of this part.

Section 200.410 Collection of unallowable costs.

Payments made for costs determined to be unallowable by either the Federal awarding agency, cognizant agency for indirect costs, or pass-through entity, either as direct or indirect costs, must be refunded (including interest) to the Federal Government in accordance with instructions from the Federal agency that determined the costs are unallowable unless Federal statute or regulation directs otherwise. See also Subpart D—Post Federal Award Requirements of this part, §§200.300 Statutory and national policy requirements through 200.309 Period of performance.

Section 200.516 Audit findings, states in part:

- (a) *Audit findings reported.* The auditor must report the following as audit findings in a schedule of findings and questioned costs:
- (1) Significant deficiencies and material weaknesses in internal control over major programs and significant instances of abuse relating to major programs. The auditor's determination of whether a deficiency in internal control is a significant deficiency or material weakness for the purpose of reporting an audit finding is in relation to a type of compliance requirement for a major program identified in the Compliance Supplement.
 - (3) Known questioned costs that are greater than \$25,000 for a type of compliance requirement for a major program. Known questioned costs are those specifically identified by the auditor. In evaluating the effect of questioned costs on the opinion on compliance, the auditor considers the best estimate of total costs questioned (likely questioned costs), not just the questioned costs specifically identified (known questioned costs). The auditor must also report known questioned costs when likely questioned costs are greater than \$25,000 for a type of compliance requirement for a major program. In reporting questioned costs, the auditor must include information to provide proper perspective for judging the prevalence and consequences of the questioned costs.

The American Institute of Certified Public Accountants defines significant deficiencies and material weaknesses in internal controls over compliance in its *Codification of Statements on Auditing Standards*, section 935, Compliance Audits, as follows:

.11 For purposes of adapting GAAS to a compliance audit, the following terms have the meanings attributed as follows: ...

Deficiency in internal control over compliance. A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance on a timely basis. A deficiency in design exists when (a) a control necessary to meet the control objective is missing, or (b) an existing control is not properly designed so that, even if the control operates as designed, the control objective would not be met. A deficiency in operation exists when a properly designed

control does not operate as designed or the person performing the control does not possess the necessary authority or competence to perform the control effectively.

Material weakness in internal control over compliance. A deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a compliance requirement will not be prevented, or detected and corrected, on a timely basis. In this section, a reasonable possibility exists when the likelihood of an event occurring is either reasonably possible or probable as defined as follows:

Reasonably possible. The chance of the future event or events occurring is more than remote but less than likely.

Probable. The future event or events are likely to occur.

Significant deficiency in internal control over compliance. A deficiency, or a combination of deficiencies, in internal control over compliance that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

The Department of Early Learning, 3.07 Federal Timekeeping Policies and Procedures, states in part:

Positive Time and Attendance Record (PTAR). Employees who work on multiple cost activities will be required to confirm their Time and Attendance bi-monthly through the use of a PTAR which must meet the following standards:

- Must be completed each pay period.
- Must reflect an after-the-fact distribution of the actual activity of the employee.
- Must account for the total activity for which the employee is compensated.
- The employee will prepare these forms after the work has been completed and will account for all hours for which the employee was compensated.
- Must be approved a responsible supervisory official who has firsthand knowledge of the activities performed by the employee.
- Every July and February the grant department will audit the forms for completion and accuracy as appropriate.
- If at any time the employee and/or supervisor notes that an employee's duties are no longer solely committed to a single cost activity, the employee will immediately be determined to be working on multiple cost activities and will begin the process to document Time and Attendance on a Positive Time and Attendance Record (PTAR).

Semi-annual Certification. For employees who work solely in a single federal award or a single cost activity, will have their Time and Attendance confirmed twice annually through the use of a Semi-Annual Certification. Semi-annual certification must meet the following standards:

- The certificate must be provided to the payroll office semi-annually and must reflect the appropriate pay periods.

- The certificate must be approved by the employee's responsible supervisory official who has firsthand knowledge of the activities performed by the employee in the prior six-month period.
- The certificate must reflect an after-the-fact distribution of the actual activity of each employee.
- Semi-Annual Certification will include the names of all individuals paid through a specified federal grant who have worked on a single cost activity in the previous six month period.
- These certifications will be distributed by the grant department for the time period of July 1st – December 31st and January 1st – June 30th.
- If at any time the employee and/or supervisor notes that an employee's duties are no longer solely committed to a single cost activity, the employee will immediately be determined to be working on multiple cost activities and will begin the process to document Time and Attendance on a Positive Time and Attendance Record (PTAR).

Step-by-Step Process: Semi-Annual Certification

Employees who are funded by a single federal grant or cost objective must complete a Semi- Annual certification of time spent in the activity to which they are charged in lieu of a semi- monthly Timesheet Form.

1. Provide previous months Payroll reports on the 15th of the current month. Email the report to Grant Staff when report is complete.
2. Audit and review payroll reports monthly, verifying employees coding and certificates form have been completed.
3. By the 16th of January and July, an email notification will be sent to employees who need to submit a certification. The email will include a semi-annual certification form.
4. Review, verify accuracy, resolve questions, then sign the semi-annual certification form and submit to Grants within 5 business days.
5. The receipt of semi-annual certification forms will be tracked.

2018-034 The Department of Children, Youth, and Families did not have adequate internal controls over and was not compliant with requirements to ensure payments to child care providers for the Child Care and Development Fund program were allowable.

Federal Awarding Agency: U.S. Department of Health and Human Services
Pass-Through Entity: None
CFDA Number and Title: 93.575 Child Care and Development Block Grant
93.596 Child Care Mandatory and Matching Funds of the Child Care and Development Fund
Federal Award Number: G1801WACCDF, G1701WACCDF, G1601WACCDF
Applicable Compliance Component: Activities Allowed or Unallowed and Allowable Costs/Cost Principles
Known Questioned Cost Amount: \$5,894

Background

The Department of Children, Youth, and Families (DCYF) (formerly the Department of Early Learning) administers the federal Child Care and Development Fund (CCDF) grant to help eligible working families pay for child care. The Department of Social and Health Services (DSHS) determines client eligibility and pays child care providers under an agreement with DCYF. Providers are paid from both the CCDF grant and the Temporary Assistance for Needy Families grant, and a payment can include funding from both programs.

DCYF is responsible for establishing policies and procedures to ensure payments are allowable. In fiscal year 2018, DCYF made 639,816 monthly child care subsidy payments to child care providers from both the CCDF and TANF grants as well as state funding. These payments totaled almost \$267 million in federal funds with over \$189 million paid with CCDF funds.

There are three child care provider types: licensed centers; licensed family homes; and family, friends and neighbor providers (FFN). Licensed centers typically operate as larger facilities, whereas licensed family homes are limited to no more than 12 children at a given time. Both centers and homes must adhere to strict licensing requirements established by DCYF and are subject to annual monitoring visits.

FFN providers are exempt from many of the licensing requirements and are not subject to routine onsite monitoring visits. These providers are limited to receiving payment for a maximum of six children in their home at a time.

Authorizations for child care

To be authorized for child care services, parents must be determined to be eligible based on their income, residency and demonstrated need based on their work schedules. Once parents are determined to be eligible, DSHS authorizes service levels. For licensed providers, the service levels are generally either 23 full-day units (up to 10 hours a day) or 30 half-day units (up to five hours a day) when

authorizing care for households with more than 110 hours of activity. Care is authorized based on need when approvable activities are less than 110 hours. FFN providers are paid by the hour and authorizations are made for either part-time care (up to 110 hours a month) or full-time care (up to 230 hours a month).

Attendance records

According to state rules, child care providers must maintain attendance records to support their billing. At a minimum, the records must include: the children's names; date(s) child care was provided; and authorized signatures, typically of a parent or guardian, documenting the times the child arrived and left care.

DCYF subsidy auditor reconciliations

Providers are not required to submit attendance records with their monthly requests for payment. DCYF has established a subsidy audit unit that randomly selects prior payments for review. Upon request, providers must submit attendance records and other supporting documentation, which are reconciled to paid invoices.

DCYF subsidy auditors completed 2,454 reconciliations during the audit period and identified 1,358 instances (55 percent) of provider overpayments that totaled \$1,037,792. The identified overpayments represented about 17 percent of the total amount of payments reviewed.

The most common reasons DCYF's reconciliations determined overpayments occurred were:

- Providers overbilled because child care was not provided.
- Providers did not submit required attendance records.
- Providers billed for the maximum amount of authorized childcare when they were not permitted to do so.

Prior audit results

In the prior audit, we reported DCYF failed to establish adequate internal controls over and was not compliant with federal requirements to ensure payments to child care providers were allowable. We have reported this condition since 2005. The most recent audit finding numbers were 2017-024, 2016-021, 2015-023, 2014-023, 2013-016, 12-28, 11-23, 10-31, 9-12 and 8-13.

Description of Condition

We found DCYF took steps to address the previous findings, but continued to lack adequate internal controls to effectively prevent and detect unallowable payments to child care providers.

We used a statistical sampling method to randomly select and examine 133 payments for child care to determine if they were allowable. We chose child care payments by totals from each of the three provider types: licensed centers, licensed family homes and FFN's. With assistance from DCYF, we requested attendance records from providers that supported the payments. We reviewed each provider's

records to determine if the payments were allowed by federal and state regulations, as well as by DCYF's policies.

We found 36 payments funded by the CCDF grant that were partially or fully unallowable. In total, we questioned \$5,894 paid by federal CCDF funds.

The reasons the overpayments occurred were:

- Attendance records were not submitted by providers in response to our request
- Providers overbilled for services not performed or not supported by attendance records
- Providers billed for overtime, field trip fees and registration fees when they did not have a written policy in place to also charge these same fees to private paying parents
- Providers were not paid the correct rate based on the child's age and region

We consider these internal control deficiencies to be a material weakness.

Cause of Condition

While the authorizations establish a maximum for what providers may bill without further approval, it does not prevent providers from billing for unallowable days, hours or services. The claim and payment system is not linked to authorizations or attendance. Child care providers must maintain attendance records and submit this supporting documentation only when it is requested.

DCYF management asserts the identified internal control weaknesses will improve with the implementation of an electronic time and attendance reporting system. DCYF has implemented an electronic attendance system that maintains electronic copies of attendance records and will potentially reduce provider errors. Licensed providers were required to start using the department's electronic attendance system or an approved third party system beginning December 1, 2018. The new reporting system will enable DCYF to perform data analysis and audit of payments. In addition, new rules and policies for providers have been written, but have not been implemented due to timing of the audit.

Effect of Condition and Questioned Costs

By not having adequate internal controls in place, DCYF increases its risk of making improper payments for child care services.

A statistical sampling method was used to randomly select the payments examined in the audit. Based on the results of our testing, we estimate the total amount of likely improper payments with federal CCDF funds to be \$28,176,448. Many of the improper payments were partially funded by state dollars. We found \$1,656 of improper state payments, which projects to a likely improper payment amount of \$7,915,754. This amount is not included in the federal questioned costs.

Our sampling methodology meets statistical sampling criteria under generally accepted auditing standards in AU-C 530.05. It is important to note that the sampling technique we used is intended to support our audit conclusions by determining if expenditures complied with program requirements in

all material respects. Accordingly, we used an acceptance sampling formula designed to provide a very high level of assurance, with a 99 percent confidence of whether exceptions exceeded our materiality threshold. Our audit report and finding reflects this conclusion. However, the likely improper payment projections are a point estimate and only represent our “best estimate of total questioned costs” as required by 2 CFR 200.516(3). To ensure a representative sample, we stratified the population by dollar amount.

We question costs when we find an agency has not complied with grant regulations or when it does not have adequate documentation to support its expenditures.

Recommendations

We recommend DCYF:

- Implement preventative internal controls over payments to providers to reduce the rate of unallowable payments
- Consult with the grantor to discuss whether the questioned costs identified in the audit should be repaid

Department’s Response

DCYF partially concurs with the SAO findings. The SAO cited that eight providers were not paid the correct rate based on their region. However, as specified in WAC 170-290-0200, centers in four counties are assigned rates for a region other than the region they are geographically located in, in order to account for market differences in these counties. Therefore, while these rates might appear to be incorrect based on the region the provider is geographically located within, the rates were paid correctly. Initially, DCYF agreed with the rate errors cited by SAO. However, after further review DCYF discovered the rates were correct. Due to the timeline of the audit, SAO and DCYF were unable to reverse these exceptions, so DCYF will work with the grantor to have these exceptions removed.

As to the Auditor’s specific recommendations, DCYF concurs and offers the following detail:

- *Implement preventative internal controls over payments to providers to reduce the rate of unallowable payments*
 - *Effective December 1, 2018, DCYF requires all licensed providers who accept subsidy to use DCYF’s electronic attendance system or an approved third party system to track attendance. DCYF’s system enables accurate, real-time recording of child care attendance, tracks daily attendance, and captures data on child care usage. FFN providers are required to use DCYF’s system or an approved third party system for tracking attendance by November 30, 2019. DCYF will continue to work to provide the ability to link third party systems to the DCYF’s system for reporting capabilities.*
 - *DCYF continues to help providers understand the authorization and billing process. DCYF is improving its billing guides, which explain billing rules and policies, to assist providers to bill correctly. The billing guides will be available in Spring 2019. DCYF is*

updating the billing training available to licensed homes and FFN providers as well. As outlined in the Tentative Agreement with SEIU 925 for 2019-2021, this training will become mandatory for licensed homes and FFN providers. DCYF continues to research options for simplifying authorization and billing.

- *A provider's use of an electronic attendance system does not prevent the provider from overbilling. However, it will allow a provider to have detailed information regarding a child's attendance to facilitate billing DCYF correctly. The electronic attendance system will produce reports that allow DCYF to conduct automated audits beginning Spring 2019.*
- *In November 2018, DCYF implemented a process that allows subsidy auditors to provide technical assistance to providers whose billing practices DCYF identifies as incorrect. DCYF will continue this practice and implement program violation rules in July 2019. The program violation rules will, among other things, exclude providers with repeat violations from receiving child care subsidy.*
- *As of October 1, 2018, new FFN providers are required to receive DCYF's full Portable Background Check (PBC) and be approved by DCYF as a provider. DCYF creates a vendor number once the provider is approved and the provider's eligibility and vendor number is communicated with DSHS. DSHS must have this vendor number and approval to create an authorization. This separation of duties creates stronger internal controls and reduces the possibility of an ineligible provider receiving an authorization for payment.*
- *Consult with the U.S. Department of Health and Human Services to discuss repaying the questioned costs, including interest*
 - *DCYF consults with the U.S. Department of Health and Human Services whenever the agency receives an audit finding from SAO. This includes conducting a case by case review and providing any additional documentation requested when the audit finding results in questioned costs of federal funds.*
 - *In addition to reviewing audit findings, DCYF has worked collaboratively with the Office of Child Care (OCC) over the past few years to review the child care rules and procedures to ensure we are supporting the expectations under the Child Care Development Fund (CCDF). DCYF rules related to the WCCC continue to be more restrictive than the CCDF rules. This creates more internal control requirements, which can lead to increased errors identified by the SAO. To mitigate this issue, DCYF continues to work with our federal partners to timely update our CCDF plan to reflect current practice.*
 - *DCYF continues to work with OCC to ensure grant spending in accordance with the CCDF federal guidelines related to removing barriers to families obtaining child care and providing continuity of care.*

Auditor’s Concluding Remarks

We thank the Department for its cooperation and assistance throughout the audit. The Department agreed with all reported exceptions multiple times at the time of the audit. Two of the eight exceptions referred to had noncompliance other than not paying the correct rate based on the child’s age and region. The remaining six payments accounted for only \$348 of the total questioned costs in the finding. We affirm our finding and will review the status of the Department’s corrective action during our next audit.

Applicable Laws and Regulations

Title 2 U.S. Code of Federal Regulations Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance) establishes the following applicable requirements:

Section 200.53 Improper Payments states:

- (a) *Improper payment* means any payment that should not have been made or that was made in an incorrect amount (including overpayments and underpayments) under statutory, contractual, administrative, or other legally applicable requirements; and
- (b) *Improper payment* includes any payment to an ineligible party, any payment for an ineligible good or service, any duplicate payment, any payment for a good or service not received (except for such payments where authorized by law), any payment that does not account for credit for applicable discounts, and any payment where insufficient or lack of documentation prevents a reviewer from discerning whether a payment was proper.

Section 200.303 Internal controls, states in part:

The non-Federal entity must:

- (a) Establish and maintain effective internal control over the Federal award that provides reasonable assurance that the non-Federal entity is managing the Federal award in compliance with Federal statutes, regulations, and the terms and conditions of the Federal award. These internal controls should be in compliance with guidance in “Standards for Internal Control in the Federal Government” issued by the Comptroller General of the United States or the “Internal Control Integrated Framework”, issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).
- (b) Comply with Federal statutes, regulations, and the terms and conditions of the Federal awards.
- (d) Take prompt action when instances of noncompliance are identified including noncompliance identified in audit findings.

Section 200.403 Factors affecting Allowability of costs.

Except where otherwise authorized by statute, costs must meet the following general criteria in order to be allowable under Federal awards.

- (a) Be necessary and reasonable for the performance of the Federal award and be allocable thereto under these principles.
- (b) Conform to any limitations or exclusions set forth in these principles or in the Federal award as to types or amount of cost items.
- (c) Be consistent with policies and procedures that apply uniformly to both federally-financed and other activities of the non-Federal entity.
- (d) Be accorded consistent treatment. A cost may not be assigned to a Federal award as a direct cost if any other cost incurred for the same purpose in like circumstances has been allocated to the Federal award as an indirect cost.
- (e) Be determined in accordance with generally accepted accounting principles (GAAP), except, for state and local governments and Indian tribes only, as otherwise provided for in this part.
- (f) Not be included as a cost or used to meet cost sharing or matching requirements of any other federally-financed program in either the current or a prior period. See also §200.306 Cost sharing or matching paragraph (b).
- (g) Be adequately documented. See also §§200.300 Statutory and national policy requirements through 200.309 Period of performance of this part.

Section 200.410 Collection of unallowable costs.

Payments made for costs determined to be unallowable by either the Federal awarding agency, cognizant agency for indirect costs, or pass-through entity, either as direct or indirect costs, must be refunded (including interest) to the Federal Government in accordance with instructions from the Federal agency that determined the costs are unallowable unless Federal statute or regulation directs otherwise. See also Subpart D— Post Federal Award Requirements of this part, §§200.300 Statutory and national policy requirements through 200.309 Period of performance.

Section 200.516 Audit findings, states in part:

- (a) *Audit findings reported.* The auditor must report the following as audit findings in a schedule of findings and questioned costs:
 - (1) Significant deficiencies and material weaknesses in internal control over major programs and significant instances of abuse relating to major programs. The auditor's determination of whether a deficiency in internal control is a significant deficiency or material weakness for the purpose of reporting an audit finding is in relation to a type of compliance requirement for a major program identified in the Compliance Supplement.
 - (2) Material noncompliance with the provisions of Federal statutes, regulations, or the terms and conditions of Federal awards related to a major program. The auditor's determination of whether a noncompliance with the provisions of Federal statutes, regulations, or the terms and conditions of Federal awards is material for the purpose of reporting an audit finding is in relation to a type of compliance requirement for a major program identified in the compliance supplement.

- (3) Known questioned costs that are greater than \$25,000 for a type of compliance requirement for a major program. Known questioned costs are those specifically identified by the auditor. In evaluating the effect of questioned costs on the opinion on compliance, the auditor considers the best estimate of total costs questioned (likely questioned costs), not just the questioned costs specifically identified (known questioned costs). The auditor must also report known questioned costs when likely questioned costs are greater than \$25,000 for a type of compliance requirement for a major program. In reporting questioned costs, the auditor must include information to provide proper perspective for judging the prevalence and consequences of the questioned costs.
- (5) The circumstances concerning why the auditor's report on compliance for each major program is other than an unmodified opinion, unless such circumstances are otherwise reported audit findings in the schedule of findings and questioned costs for Federal awards.

The American Institute of Certified Public Accountants defines significant deficiencies and material weaknesses in internal controls over compliance in its *Codification of Statements on Auditing Standards*, section 935, Compliance Audits, as follows:

- .11 For purposes of adapting GAAS to a compliance audit, the following terms have the meanings attributed as follows: ...

Deficiency in internal control over compliance. A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance on a timely basis. A deficiency in design exists when (a) a control necessary to meet the control objective is missing, or (b) an existing control is not properly designed so that, even if the control operates as designed, the control objective would not be met. A deficiency in operation exists when a properly designed control does not operate as designed or the person performing the control does not possess the necessary authority or competence to perform the control effectively.

Material weakness in internal control over compliance. A deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a compliance requirement will not be prevented, or detected and corrected, on a timely basis. In this section, a reasonable possibility exists when the likelihood of an event occurring is either reasonably possible or probable as defined as follows:

Reasonably possible. The chance of the future event or events occurring is more than remote but less than likely.

Probable. The future event or events are likely to occur.

Significant deficiency in internal control over compliance. A deficiency, or a combination of deficiencies, in internal control over compliance that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

Material noncompliance. In the absence of a definition of material noncompliance in the governmental audit requirement, a failure to follow compliance requirements or a violation of prohibitions included in the applicable compliance requirements that results in noncompliance that is quantitatively or qualitatively material, either individually or when aggregated with other noncompliance, to the affected government program.

WAC 170-290-0268, Payment discrepancies—Provider overpayments, states:

- (1) An overpayment occurs when a provider receives payment that is more than the provider is eligible to receive. Provider overpayments are established when that provider:
 - (a) Bills and receives payment for services not provided;
 - (b) Bills without attendance records that support their billing;
 - (c) Bills and receives payment for more than they are eligible to bill;
 - (d) Routinely provides care in a location other than what was approved at the time of authorization;
 - (e) With respect to license-exempt in-home/relative providers, commonly known as "family, friends, and neighbor" providers, bills the state for more than six children at one time during the same hours of care; or
 - (f) With respect to licensed or certified providers:
 - (i) Bills the state for more than the number of children they have in their licensed capacity; or
 - (ii) Is caring for a WCCC child outside their licensed allowable age range without a DEL-approved exception; or
 - (g) With respect to certified providers caring for children in a state bordering Washington:
 - (i) Is determined not to be in compliance with their state's licensing regulations; or
 - (ii) Fails to notify DSHS within ten days of any suspension, revocation, or change to their license.
- (2) DEL or DSHS will request documentation from a provider when preparing to establish an overpayment. The provider has twenty-eight consecutive calendar days from the date of the written request to supply any requested documentation.
- (3) A provider is required to repay any payments which they were not eligible to receive.
- (4) Provider overpayments defined in subsection (1) of this section are deemed as program violations as described in WAC 170-290-0277.
- (5) A provider is required to repay any overpayment made through a departmental error.

WAC 170-290-0271 Payment discrepancies—Consumer overpayments, states:

- (1) DSHS establishes overpayments for past or current consumers when the consumer:
 - (a) Received benefits in an amount greater than the consumer was eligible to receive;
 - (b) Is determined eligible at application or reapplication based on the consumer's participation in an approved activity and used benefits, but never participated in said activity;

- (c) Failed to report changes under the requirements of WAC 170-290-0031 to DSHS which result in an error in determining eligibility, amount of care authorized, or copayment;
 - (d) Used a provider who did not meet the eligibility requirements under WAC 170-290-0125;
 - (e) Received benefits for a child who was not eligible per WAC 170-290-0005, 170-290-0015 or 170-290-0020; or
 - (f) Failed to return, by the sixtieth day, the requested income verification of new employment as provided in WAC 170-290-0012.
- (2) DEL or DSHS may request documentation from a consumer when preparing to establish an overpayment. The consumer has fourteen consecutive calendar days to supply any requested documentation.
- (3) Consumers are required to repay any benefits paid by DSHS that they were not eligible to receive.

WAC 170-290-0030 Consumers' responsibilities, states in part:

When a person applies for or receives WCCC benefits, the applicant or consumer must, as a condition of receiving those benefits:

- (11) Document their child's attendance in child care by having the consumer or other person authorized by the consumer to take the child to or from the child care:
- (a) If the provider uses a paper attendance record, sign the child in on arrival and sign the child out at departure, using their full signature and writing the time of arrival and departure; or
 - (b) Record the child's attendance using an electronic system if used by the provider;

WAC 170-290-0034 Providers' responsibilities, states:

Child care providers who accept child care subsidies must do the following:

- (1) Comply with:
- (a) All of the DEL child care licensing or certification requirements as provided in chapter 170-295, 170-296A, or 170-297 WAC, for child care providers who are licensed or certified; or
 - (b) All of the requirements in WAC 170-290-0130 through 170-290-0167, 170-290-0250, and 170-290-0268, for child care providers who provide in-home/relative care;
- (2) Report pending charges or convictions to DSHS as provided in:
- (a) Chapter 170-295, 170-296A, or 170-297 WAC, for child care providers who are licensed or certified; or
 - (b) WAC 170-290-0138 (2) and (3), for child care providers who provide in-home/relative care;
- (3) Keep complete and accurate daily attendance records for children in their care, and allow access to DEL to inspect attendance records during all hours in which authorized child care is provided as follows:
- (a) Current attendance records (including records from the previous twelve months) must be available immediately for review upon request by DEL.

- (b) Attendance records older than twelve months to five years must be provided to DSHS or DEL within two weeks of the date of a written request from either department. Beginning July 1, 2017, or upon ratification of the 2017-19 collective bargaining agreement with SEIU 925, whichever occurs later, the records must be provided within twenty-eight consecutive calendar days of the date of a written request from either department.
- (c) Failure to make available attendance records as provided in this subsection may:
 - (i) Result in the immediate suspension of the provider's subsidy payments; and
 - (ii) Establish a provider overpayment as provided in WAC 170-290-0268;
- (4) Keep receipts for billed field trip/quality enhancement fees as follows:
 - (a) Receipts from the previous twelve months must be available immediately for review upon request by DEL;
 - (b) Receipts from one to five years old must be provided to DSHS or DEL within two weeks of the date of a written request from either department;
- (5) Allow consumers access to their child at all times while the child is in care;
- (6) Collect copayments directly from the consumer or the consumer's third-party payor, and report to DSHS if the consumer has not paid a copayment to the provider within the previous sixty days;
- (7) Follow billing procedures:
 - (a) As described in the most current version of "Child Care Subsidies: A Guide for Licensed and Certified Family Home Child Care Providers,"; or
 - (b) As described in the most current version of "Child Care Subsidies: A Guide for Family, Friends and Neighbors Child Care Providers"; or
 - (c) As described in the most current version of "Child Care Subsidies: A Guide for Licensed and Certified Child Care Centers."
- (8) Not claim a payment in any month a child has not attended at least one day within the authorization period in that month.
- (9) Invoice the state no later than one calendar year after the actual date of service;
- (10) For both licensed and certified providers and in-home/relative providers, not charge subsidized families the difference between the provider's customary rate and the maximum allowed state rate; and
- (11) For licensed and certified providers, not charge subsidized families for:
 - (a) Registration fees in excess of what is paid by subsidy program rules;
 - (b) Absent days on days in which the child is scheduled to attend and authorized for care;
 - (c) Handling fees to process consumer copayments, child care services payments, or paperwork;
 - (d) Fees for materials, supplies, or equipment required to meet licensing rules and regulations; or
 - (e) Child care or fees related to subsidy billing invoices that are in dispute between the provider and the state.

WAC 170-290-0138 In-home/relative providers—Responsibilities, states in part:

An in-home/relative provider must:

- (6) Bill only for actual hours of care provided. Those hours:

- (a) Must be authorized by DSHS;
 - (b) Must be used by the consumer; and
 - (c) Can be claimed whether or not the consumer is present during the hours of care.
- (7) Bill for no more than six children at one time during the same hours of care;
- (8) Track attendance documenting the days and hours of care provided and keep records for five years:
- (a) If paper attendance records are used, the provider must have the consumer sign and date the attendance records at least weekly, verifying the accuracy of the dates and times.
 - (b) Providers may use an electronic attendance system as provided in WAC 170-290-0139 to record attendance in lieu of a paper sign-in record;
- (9) Repay any overpayments under WAC 170-290-0268; and

WAC 170-290-0190 WCCC benefit calculations, states:

- (1) The amount of care a consumer may receive is determined by DSHS at application or reapplication. The consumer does not need to be in approved activities or a reported activity schedule, except at application or reapplication. Once the care is authorized, the amount will not be reduced during the eligibility period unless:
- (a) The consumer requests the reduction;
 - (b) The care is for a school-aged child as described in subsection (3) of this section; and
 - (c) Incorrect information was given at application or reapplication according to WAC 170-290-0030.
- (2) To determine the amount of weekly hours of care needed, DSHS will review:
- (a) The consumer's participation in approved activities per WAC 170-290-0040, 170-290-0045, 170-290-0050, and 170-290-0055;
 - (b) The number of hours the child attends school, including home school, and reduce the amount of care;
 - (c) In a two parent household, the days and times the activities overlap, and only authorize care during those times;
 - (d) The parent, in a two parent household, who is not able to care for the child, as defined in WAC 170-290-0020, and exclude the activity requirements; and
 - (e) When a consumer requests and verifies the need for increased care, DSHS will increase the care for the remainder of the eligibility period.
- (3) Determining full-time care for a family using licensed providers:
- (a) Twenty-three full-day units per month will be authorized for one hundred ten hours of activity or more each month when the child needs care five or more hours per day;
 - (b) Thirty half-day units per month will be authorized for one hundred ten hours of activity or more each month when the child needs care less than five hours per day;
 - (c) Thirty half-day units per month will be authorized during the school year for a school-aged child who needs care less than five hours per day;
 - (d) Forty-six half-day units will be authorized during the months of July and August for a school-aged child who needs five or more hours of care;
 - (e) Twenty-three full-day units will be authorized during the school year for a school-aged child who needs care five or more hours per day;

- (f) Supervisor approval is required for additional days of care that exceeds twenty-three full days or thirty half days; and
 - (g) Care cannot exceed sixteen hours per day, per child.
- (4) Determining full-time care for a family using in-home/relative providers (family, friend and neighbors).
- (a) Two hundred thirty hours of care will be authorized for one hundred ten hours of activity or more each month when the child needs care five or more hours per day;
 - (b) One hundred fifteen hours of care will be authorized for one hundred ten hours of activity or more each month when the child needs care less than five hours per day;
 - (c) One hundred fifteen hours of care will be authorized during the school year for a school-aged child who needs care less than five hours per day and the provider will be authorized contingency hours each month, up to a maximum of two hundred thirty hours;
 - (d) Two hundred thirty hours of care will be authorized during the school year for a school-aged child who needs care five or more hours in a day;
 - (e) Supervisor approval is required for hours of care that exceed two hundred thirty hours; and
 - (f) Care cannot exceed sixteen hours per day, per child.
- (5) Determining part-time care for a family using licensed providers and the activity is less than one hundred ten hours per month.
- (a) A full-day unit will be authorized for each day of care that exceeds five hours;
 - (b) A half-day unit will be authorized for each day of care that is less than five hours; and
 - (c) A half-day unit will be authorized for each day of care for a school-aged child, not to exceed thirty half days.
- (6) Determining part-time care for a family using in-home/relative providers (family, friend and neighbors).
- (a) Under the provisions of subsection (2) of this section, DSHS will authorize the number of hours of care needed per month when the activity is less than one hundred ten hours per month; and
 - (b) When the provider claims contingency hours, the total number of authorized hours and contingency hours claimed cannot exceed two hundred thirty hours per month.
- (7) DSHS determines the allocation of hours or units for families with multiple providers based upon the information received from the parent.
- (8) DSHS may authorize more than the state rate and up to the provider's private pay rate if:
- (a) The parent is a WorkFirst participant; and
 - (b) Appropriate child care, at the state rate, is not available within a reasonable distance from the approved activity site. "Appropriate" means licensed or certified child care under WAC 170-290-0125, or an approved in-home/relative provider under WAC 170-290-0130. "Reasonable distance" is determined by comparing distances other local families must travel to access appropriate child care.
- (9) Other fees DSHS may authorize to a provider are:
- (a) Registration fees;
 - (b) Field trip fees;
 - (c) Nonstandard hours bonus;

- (d) Overtime care to a licensed provider who has a written policy to charge all families, when care is expected to exceed ten hours in a day; and
 - (e) Special needs rates for a child.
- (10) In-home/relative providers who are paid child care subsidies to care for children receiving WCCC benefits cannot receive those benefits for their own children during the hours in which they provide subsidized child care.

WAC 170-290-0245 Registration fees, states:

- (1) DSHS may pay licensed or certified child care providers and DEL contracted seasonal day camps a registration fee when:
- (a) A child is first enrolled by the consumer for child care with a provider;
 - (b) A consumer enrolls their child with a new child care provider during their eligibility period; or
 - (c) A child has more than a sixty-day break in child care services with the same provider, and it is the provider's policy to charge all parents this fee when there is a break in service.
- (2) A registration fee will be paid only once per calendar year for children who are cared for by the same provider, even if the provider receives subsidy payments under different subsidy programs during this time period for the enrolled children, unless there is a break of sixty days or more as provided in subsection (1)(c) of this section.

WAC 170-290-0247 Field trip/quality enhancement fees, states:

- (1) DSHS pays licensed or certified family home child care providers a monthly field trip/quality enhancement fee up to thirty dollars per child or the provider's actual cost for the field trip, whichever is less, only if the fee is required of all parents whose children are in the provider's care. DEL-licensed or certified child care centers and school-age centers are not eligible to receive the field trip/quality enhancement fee.
- (2) The field trip/quality enhancement fee is to cover the provider's actual expenses for:
- (a) Admission;
 - (b) Enrichment programs and/or ongoing lessons;
 - (c) Public transportation or mileage reimbursement at the state office of financial management rate for the use of a private vehicle;
 - (d) The cost of hiring a nonemployee to provide an activity at the child care site in-house field trip activity; and
 - (e) The purchase or development of a prekindergarten curriculum.
- (3) The field trip/quality enhancement fee shall not cover fees or admission costs for adults on field trips, or food purchased on field trips.

WAC 170-290-0249 Nonstandard hours bonus, states:

- (1) A consumer's provider may receive a nonstandard hours bonus (NSHB) payment of seventy-five dollars per child per month for care provided if:
- (a) The provider is licensed or certified;
 - (b) The provider provides at least thirty hours of non-standard hours care during one month; and

- (c) The total cost of the NSHB to the state does not exceed the amount appropriated for this purpose by the legislature for the current state fiscal year.
- (2) Nonstandard hours are defined as:
 - (a) Before 6 a.m. or after 6 p.m.;
 - (b) Any hours on Saturdays and Sundays; and
 - (c) Any hours on legal holidays, as defined in RCW 1.16.050.

2018-035

The Department of Children, Youth, and Families did not have adequate internal controls over and did not comply with health and safety requirements for the Child Care and Development Fund program.

Federal Awarding Agency: U.S. Department of Health and Human Services
Pass-Through Entity: None
CFDA Number and Title: 93.575 Child Care and Development Block Grant
93.596 Child Care Mandatory and Matching Funds of the Child Care and Development Fund
Federal Award Number: G1801WACCDF, G1701WACCDF, G1601WACCDF
Applicable Compliance Component: Special Tests and Provisions – Health and Safety Requirements
Known Questioned Cost Amount: \$1,678

Background

The Department of Children, Youth, and Families (DCYF), formerly the Department of Early Learning, administers the federal Child Care and Development Fund (CCDF) grant to help eligible working families pay for childcare. Although DCYF is the lead agency for the CCDF program, the Department of Social and Health Services (DSHS) has responsibility over certain health and safety requirements under an agreement with DCYF.

In fiscal year 2018, the agencies paid about \$189 million in CCDF federal funding to childcare providers. DCYF is responsible for ensuring providers meet licensing standards, which includes ensuring background checks are performed for all staff with direct access to children.

Provider inspections

DCYF conducts annual, unannounced inspections of licensed providers to verify if required health and safety standards are being met and requires providers to address any identified issues. DCYF licensors document inspections using a monitoring checklist. If a provider has no recent complaints or identified noncompliance, and has received a full checklist review in the past three years, an abbreviated checklist may be used. Otherwise, the licensor must use a full review checklist.

When health and safety infractions are identified, licensors document them on a Facility Licensing Compliance Agreement (FLCA). The FLCA identifies the areas of provider noncompliance and establishes deadlines for correcting them. Providers must submit a corrective action plan or resolution activity to their licensor.

If an inspection was attempted, but the provider was not present, the licensor must follow up and conduct the inspection within 30 days of the due date. If after the licensor follow up DCYF is still unable to schedule another inspection, the licensor consults with their supervisor for a decision on conducting any further inspection attempts.

Common examples of noncompliance identified by licensors are:

- Providers that exceed the required staff-to-child ratios
- Providers that did not maintain accurate or complete attendance logs
- Providers missing training or certification requirements
- Health and safety hazards

When serious health and safety violations are identified, licensors must conduct an unannounced re-check of the facility within 10 business days. Less serious non-compliance issues must be addressed within 30 days. If the provider does not resolve a noncompliance issue, DCYF may impose sanctions, issue fines, or suspend or revoke the provider's license.

In June 2017, DCYF replaced its current system with a new electronic system (WA Compass) to allow licensing staff to make more timely updates and streamline their process for performing monitoring visits.

Background checks

DSHS ensures Family, Friends, & Neighbors (FFNs) providers, which are exempt from licensing requirements, pass background checks before becoming providers, and at least every two years or when there is a 30-day break in service in providing care.

Registered sex offender cross match

As part of the monitoring process, DSHS will perform a cross match to identify any in-home or FFN providers that have a registered sex offender living in the home where care is provided. The cases that involve in-home providers are investigated by DCYF, and the cases that involve FFNs are investigated by DSHS. If it is determined that a registered sex offender is in the home, the provider is permanently disqualified from providing care.

In prior audits, we reported DCYF did not have adequate internal controls over and did not comply with health and safety requirements. The prior finding numbers were 2017-025, 2016-022 and 2015-024.

Description of Condition

We found DCYF did not have adequate internal controls over and did not comply with requirements to ensure providers met health and safety requirements.

Provider inspections

In state fiscal year 2018, DCYF regulated 4,538 licensed providers. DCYF staff informed us that 1,073 (24 percent) of all licensed providers were overdue on their yearly inspections.

We used a statistical sampling method to randomly select and examine records for 58 licensed providers who received federal CCDF payments during state fiscal year 2018 to determine if inspections were conducted as required. We found:

- Two (3 percent) inspections were overdue and not conducted by June 30, 2018.
- Ten (17 percent) inspections were performed late by up to nine months.

We reviewed the provider's prior visit history to determine if the licensor used the appropriate monitoring checklist. We found nine instances (16 percent) when licensors did not use the full inspection checklist as required.

We examined DCYF's response to serious violations documented during inspections and found 12 instances (21 percent) when there was not sufficient documentation to show follow-up was performed adequately, or promptly for violations of health, safety or well-being of children. Some examples of these serious violations were:

- General health and safety hazards to the children
- Lack of background check documentation
- Inadequate supervision of children

We also found circumstances that required a follow-up visit, but for which licensors accepted and relied on provider attestations in their FLCA in place of the onsite inspections to resolve issues.

Additionally, during our testing of childcare subsidy payments to childcare providers, we randomly selected and examined 133 payments to determine if they were allowable. We reviewed attendance records to determine if they complied with health and safety requirements.

We found:

- Fifty-four of 133 attendance records did not support time billed, were missing parent/guardians' full signatures for sign in/out as applicable or did not respond to our request for records.
- Nine of 60 licensed homes' and FFN providers' attendance records (or lack thereof) did not support that the provider was at or under capacity (fewer than 12 children at one time for a licensed home) or not billing over allowable limits (six CCDF funded children for an FFN).

Background checks

We used a statistical sampling method to randomly select 59 FFN providers to examine whether DSHS performed background checks as required. We found two background checks were not performed before the provider became eligible and received payments for providing care to children.

Registered sex offender cross match

Of the 12 cases that were reviewed by DSHS during fiscal year 2018, DSHS identified one FFN that was providing care to three children while a registered sex offender lived in the home. DSHS immediately stopped services for one child. The other two children were allowed to continue receiving

care for nine days totaling \$355, when services were then stopped. Although these payments were made outside of our audit period, we used them to confirm that care was provided after the issue was identified. These payments are not included in the known questioned cost amount.

We consider these internal control deficiencies to be a material weakness.

Cause of Condition

DCYF said it was unable to complete all licensing visits promptly for the following reasons:

- Transition to a new licensing management system
- Turnover of licensing staff
- It was in the process of transitioning to a new set of aligned licensing standards scheduled to go into effect in the fall of 2019. DCYF acknowledged that rules in effect during the audit period were less conducive to timely completion of licensing visits.
- Some providers refused the licensor access

Management did not effectively monitor to ensure licensors completed required monitoring and follow-up visits promptly.

DSHS said that Washington Administrative Code require 10 days' notice be given when closing a provider. However, one child's authorization was closed immediately while the second family was given the 10-day notice.

Effect of Condition and Questioned Costs

Provider inspections

When inspections are not conducted, or are conducted late, health and safety violations are less likely to be detected by DCYF promptly, if at all.

Further, we found that four inspection records (7 percent) we reviewed identified noncompliance with a health or safety issue that had also been identified as noncompliant in the prior inspection. While those cases were not ones in which DCYF also failed to conduct timely visits, they illustrate the importance of timeliness in addressing repeat issues. By not following up on violations promptly, the DCYF cannot be sure these issues have been corrected. Health and safety, background check and over-capacity/over-ratio violations might put children in jeopardy for harm, neglect, and unhealthy emotional and cognitive development environments.

Background checks

The two providers who were determined to be eligible and received payments before their background checks were approved received \$1,678 in improper payments with federal funds. Because a statistical sampling method was used to select the providers examined, we estimate the amount of likely federal improper payments to be \$214,660. Additionally, the providers were improperly paid \$32 in state funds, and we estimate likely state funded improper payments of \$4,096.

Registered sex offender cross match

DSHS allowed two children to receive care for nine days in a home where a registered sex offender lived. Although the Department is not required to license or routinely monitor FFN providers, both Departments put two children at risk for harm and neglect when they did not immediately stop care.

Our sampling methodology meets statistical sampling criteria under generally accepted auditing standards in AU-C 530.05. It is important to note that the sampling technique we used is intended to support our audit conclusions by determining if expenditures complied with program requirements in all material respects. Accordingly, we used an acceptance sampling formula designed to provide a high level of assurance, with a 95 percent confidence of whether exceptions exceeded our materiality threshold. Our audit report and finding reflects this conclusion. However, the likely improper payment projections are a point estimate and only represent our “best estimate of total questioned costs” as required by 2 CFR 200.516(3).

We question costs when we find an agency has not complied with grant regulations or when it does not have adequate documentation to support its expenditures.

Recommendations

We recommend the Departments:

- Ensure management follows policy and procedures to ensure all visits are performed on time and in compliance with regulations
- Ensure aligned licensing standards are implemented promptly and that staff follow them
- Ensure staff sufficiently document the results of follow-up visits when serious violations are identified
- Ensure providers are not approved to provide care until all required background checks have been completed
- Ensure care is immediately stopped when it is determined a registered sex offender is living in a home that is providing childcare for children that do not reside in the home
- Consult with the grantor to discuss whether the questioned costs identified in the audit should be repaid

Department’s Response

The Department concurs with this finding and is strongly committed to ensuring the health, safety, and well-being of all children in licensed child care.

As to the Auditor’s specific recommendations, DCYF concurs and offers the following detail:

- *Ensure management follows policy and procedures to ensure all visits are performed on time and in compliance with regulations and ensure aligned licensing standards are implemented promptly and that staff follow them*
 - *DCYF has implemented new monitoring and compliance agreement policies and procedures to clarify language for the use of a full checklist every three years, to clarify*

when a site visit is needed, what methods of verifying compliance can be used, and the timelines for documentation. The Department has trained all child care licensing staff regarding these requirements.

- *DCYF continues to revise all licensing policies, procedures, and tasks to ensure they align with current state and federal rules and regulations. As DCYF moves toward the alignment of Family Home and Child Care Center licensing rules in Washington Administrative Code (WAC), the policies are being reviewed and revised as necessary to assure that they remain aligned with current state and federal rules and regulations and that all staff are trained prior to implementation of the updated WAC in August 2019.*
- *DCYF is currently in the process of preparing for the implementation of the aligned Family Home and Child Care Center WAC to be effective August 1, 2019. This alignment process is in response to the demands of the legislature and to the needs of the provider community. In preparation for this implementation, all child care licensing staff are completing mandatory training on the updated WAC components and how policies, procedures, and tasks will change as a result of the updated standards. New checklists, which will allow for more focused monitoring, will be introduced with the aligned WAC. In addition, an inspection report will be generated which will more clearly delineate the areas of high risk that need a follow up visit.*
- *Ensure staff sufficiently document the results of follow-up visits when serious violations are identified*
 - *DCYF has implemented a new IT system, WA COMPASS, for use by licensing staff in managing and conducting licensing inspections including monitor visits. This system has improved data integrity, streamlined staff work processes, and provides electronic reminders to licensing staff and supervisors. In future enhancements to the system, a method to monitor due dates for follow up visits on health and safety issues is anticipated. During the interim, licensing staff and supervisors have been trained on the requirements to document the results of follow up visits in a timely manner. Supervisors are currently able to run a report to see if dates are missed so they can address those concerns with licensing staff.*
- *Ensure providers are not approved to provide care until all required background checks have been completed*
 - *As of October 1, 2018, new FFN providers are required to receive DCYF's full Portable Background Check (PBC) and be approved by DCYF as a provider. DCYF creates a vendor number once the provider is approved and the provider's eligibility and vendor number is communicated with DSHS. DSHS must have this vendor number and approval to create an authorization.*
- *Ensure care is immediately stopped when it is determined a registered sex offender is living in a home that is providing childcare for children that do not reside in the home*
 - *DCYF has clarified and implemented a policy revision to allow for termination without notice to providers when there is an unsafe environment or when a provider becomes ineligible. The Department is also working on updating the WAC language that covers these situations. DSHS has provided updated training to staff on CCDF policies.*

- *Consult with the grantor to discuss whether the questioned costs identified in the audit should be repaid*
 - *If the federal grantor contacts the Department regarding questioned costs that should be repaid, the Department will confirm these costs and will take appropriate action*

Auditor’s Concluding Remarks

We thank the Department for its cooperation and assistance throughout the audit. We will review the status of the Department’s corrective action during our next audit.

Applicable Laws and Regulations

Title 2 U.S. Code of Federal Regulations Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance) establishes the following applicable requirements:

Section 200.53 Improper Payments states:

- (a) *Improper payment* means any payment that should not have been made or that was made in an incorrect amount (including overpayments and underpayments) under statutory, contractual, administrative, or other legally applicable requirements; and
- (b) *Improper payment* includes any payment to an ineligible party, any payment for an ineligible good or service, any duplicate payment, any payment for a good or service not received (except for such payments where authorized by law), any payment that does not account for credit for applicable discounts, and any payment where insufficient or lack of documentation prevents a reviewer from discerning whether a payment was proper.

Section 200.303 Internal controls, states in part:

The non-Federal entity must:

- (a) Establish and maintain effective internal control over the Federal award that provides reasonable assurance that the non-Federal entity is managing the Federal award in compliance with Federal statutes, regulations, and the terms and conditions of the Federal award. These internal controls should be in compliance with guidance in “Standards for Internal Control in the Federal Government” issued by the Comptroller General of the United States or the “Internal Control Integrated Framework”, issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).
- (b) Comply with Federal statutes, regulations, and the terms and conditions of the Federal awards.
- (d) Take prompt action when instances of noncompliance are identified including noncompliance identified in audit findings.

Section 200.403 Factors affecting Allowability of costs.

Except where otherwise authorized by statute, costs must meet the following general criteria in order to be allowable under Federal awards.

- (a) Be necessary and reasonable for the performance of the Federal award and be allocable thereto under these principles.
- (b) Conform to any limitations or exclusions set forth in these principles or in the Federal award as to types or amount of cost items.
- (c) Be consistent with policies and procedures that apply uniformly to both federally-financed and other activities of the non-Federal entity.
- (d) Be accorded consistent treatment. A cost may not be assigned to a Federal award as a direct cost if any other cost incurred for the same purpose in like circumstances has been allocated to the Federal award as an indirect cost.
- (e) Be determined in accordance with generally accepted accounting principles (GAAP), except, for state and local governments and Indian tribes only, as otherwise provided for in this part.
- (f) Not be included as a cost or used to meet cost sharing or matching requirements of any other federally-financed program in either the current or a prior period. See also §200.306 Cost sharing or matching paragraph (b).
- (g) Be adequately documented. See also §§200.300 Statutory and national policy requirements through 200.309 Period of performance of this part.

Section 200.410 Collection of unallowable costs.

Payments made for costs determined to be unallowable by either the Federal awarding agency, cognizant agency for indirect costs, or pass-through entity, either as direct or indirect costs, must be refunded (including interest) to the Federal Government in accordance with instructions from the Federal agency that determined the costs are unallowable unless Federal statute or regulation directs otherwise. See also Subpart D—Post Federal Award Requirements of this part, §§200.300 Statutory and national policy requirements through 200.309 Period of performance.

Section 200.516 Audit findings, states in part:

- (a) *Audit findings reported.* The auditor must report the following as audit findings in a schedule of findings and questioned costs:
 - (1) Significant deficiencies and material weaknesses in internal control over major programs and significant instances of abuse relating to major programs. The auditor's determination of whether a deficiency in internal control is a significant deficiency or material weakness for the purpose of reporting an audit finding is in relation to a type of compliance requirement for a major program identified in the Compliance Supplement.
 - (2) Material noncompliance with the provisions of Federal statutes, regulations, or the terms and conditions of Federal awards related to a major program. The auditor's determination of whether a noncompliance with the provisions of Federal statutes, regulations, or the terms and conditions of Federal awards is material for the purpose

of reporting an audit finding is in relation to a type of compliance requirement for a major program identified in the compliance supplement.

- (3) Known questioned costs that are greater than \$25,000 for a type of compliance requirement for a major program. Known questioned costs are those specifically identified by the auditor. In evaluating the effect of questioned costs on the opinion on compliance, the auditor considers the best estimate of total costs questioned (likely questioned costs), not just the questioned costs specifically identified (known questioned costs). The auditor must also report known questioned costs when likely questioned costs are greater than \$25,000 for a type of compliance requirement for a major program. In reporting questioned costs, the auditor must include information to provide proper perspective for judging the prevalence and consequences of the questioned costs.
- (5) The circumstances concerning why the auditor's report on compliance for each major program is other than an unmodified opinion, unless such circumstances are otherwise reported audit findings in the schedule of findings and questioned costs for Federal awards.

The American Institute of Certified Public Accountants defines significant deficiencies and material weaknesses in internal controls over compliance in its *Codification of Statements on Auditing Standards*, section 935, Compliance Audits, as follows:

.11 For purposes of adapting GAAS to a compliance audit, the following terms have the meanings attributed as follows: ...

Deficiency in internal control over compliance. A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance on a timely basis. A deficiency in design exists when (a) a control necessary to meet the control objective is missing, or (b) an existing control is not properly designed so that, even if the control operates as designed, the control objective would not be met. A deficiency in operation exists when a properly designed control does not operate as designed or the person performing the control does not possess the necessary authority or competence to perform the control effectively.

Material weakness in internal control over compliance. A deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a compliance requirement will not be prevented, or detected and corrected, on a timely basis. In this section, a reasonable possibility exists when the likelihood of an event occurring is either reasonably possible or probable as defined as follows:

Reasonably possible. The chance of the future event or events occurring is more than remote but less than likely.

Probable. The future event or events are likely to occur.

Significant deficiency in internal control over compliance. A deficiency, or a combination of deficiencies, in internal control over compliance that is less severe than a

material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

Material noncompliance. In the absence of a definition of material noncompliance in the governmental audit requirement, a failure to follow compliance requirements or a violation of prohibitions included in the applicable compliance requirements that results in noncompliance that is quantitatively or qualitatively material, either individually or when aggregated with other noncompliance, to the affected government program.

45 Code of Federal Regulations section 98.40 Compliance with applicable State and local regulatory requirements, states:

(a) Lead Agencies shall:

(1) Certify that they have in effect licensing requirements applicable to child care services provided within the area served by the Lead Agency;

(2) Provide a detailed description of the requirements under paragraph (a)(1) of this section and of how they are effectively enforced.

(b) (1) This section does not prohibit a Lead Agency from imposing more stringent standards and licensing or regulatory requirements on child care providers of services for which assistance is provided under the CCDF than the standards or requirements imposed on other child care providers.

(2) Any such additional requirements shall be consistent with the safeguards for parental choice in § 98.30(f).

45 Code of Federal Regulations section 98.41 Health and safety requirements, states:

(a) Although the Act specifically states it does not require the establishment of any new or additional requirements if existing requirements comply with the requirements of the statute, each Lead Agency shall certify that there are in effect, within the State (or other area served by the Lead Agency), under State, local or tribal law, requirements designed to protect the health and safety of children that are applicable to child care providers of services for which assistance is provided under this part. Such requirements shall include:

(1) The prevention and control of infectious diseases (including immunizations). With respect to immunizations, the following provisions apply:

(i) As part of their health and safety provisions in this area, States and Territories shall assure that children receiving services under the CCDF are age-appropriately immunized. Those health and safety provisions shall incorporate (by reference or otherwise) the latest recommendation for childhood immunizations of the respective State or territorial public health agency.

(ii) Notwithstanding paragraph (a)(1)(i) of this section, Lead Agencies may exempt:

(A) Children who are cared for by relatives (defined as grandparents, great grandparents, siblings (if living in a separate residence), aunts, and uncles);

(B) Children who receive care in their own homes;

(C) Children whose parents object to immunization on religious grounds; and

- (D) Children whose medical condition contraindicates immunization;
- (iii) Lead Agencies shall establish a grace period in which children can receive services while families are taking the necessary actions to comply with the immunization requirements;
- (2) Building and physical premises safety; and
- (3) Minimum health and safety training appropriate to the provider setting.
- (b) Lead Agencies may not set health and safety standards and requirements under paragraph (a) of this section that are inconsistent with the parental choice safeguards in § 98.30(f).
- (c) The requirements in paragraph (a) of this section shall apply to all providers of child care services for which assistance is provided under this part, within the area served by the Lead Agency, except the relatives specified in paragraph (e) of this section.
- (d) Each Lead Agency shall certify that procedures are in effect to ensure that child care providers of services for which assistance is provided under this part, within the area served by the Lead Agency, comply with all applicable State, local, or tribal health and safety requirements described in paragraph (a) of this section.
- (e) For the purposes of this section, the term “child care providers” does not include grandparents, great grandparents, siblings (if such providers live in a separate residence), aunts, or uncles, pursuant to § 98.2.

We identified the following Washington Administrative Codes relevant to Health and Safety:

- WAC 170-290-0034 Provider’s Responsibilities
- WAC 170-290-0143 In-home/relative providers—Background checks—Required persons
- WAC 170-290-0138 In-home/relative providers – Responsibilities
- WAC 170-290-0160 In-home/relative providers – Background checks – Disqualified Providers
- WAC 170-290-0268 Payment discrepancies – Provider overpayments
- WAC 170-295-0030 Eligibility to receive state child care subsidies
- WAC 170-295-7030 Attendance records
- WAC 170-296A-1050 The licensee
- WAC 170-296A-1075 Child care subsidy
- WAC 170-296A-1410 Department inspection
- WAC 170-296A-8000 Facility licensing compliance agreements
- WAC 170-296A-8025 Time period for correcting a violation
- WAC 170-296A-8175 Violations—Enforcement action
- WAC 170-297-1410 Department inspection
- WAC 170-297-8000 Facility licensing compliance agreements
- WAC 170-297-8025 Time period for correcting a violation
- WAC 170-297-8175 Violations—Enforcement action

The Department of Early Learning Child Care Licensing Policies and Procedures, 10.1.8 Monitoring Visits Procedure, states in part:

2. A full checklist (10.9.3.5 Family Home Checklist, 10.9.4.6 Child Care Center Checklist, or 10.9.4.11 SA Checklist) must be used at least once every 3 years effective January 1, 2016. When the file is up for the three year review this must be verified and/or completed.

5. Monitoring visits must be unannounced, unless approved by a supervisor. If children are not in care, the monitoring visit can be conducted with the expectation that the licensor will return within 30 days to observe the program with children present. If children are not in care during the follow-up visit, the licensor must consult with their supervisor for a decision on conducting further visits.

6. If the licensee is temporarily closed a visit must not be conducted. This visit must be documented as “Attempted” in the provider notes.

7. Attempted visits must be followed up and conducted within 30 calendar days. If a follow-up visit cannot be conducted, the licensor must consult with their supervisor for a decision on conducting any further visits.

8. A family home child care, child care center and school age program monitor visit must occur every 12 months – within 90 days prior to the yearly due date. The Monitoring Visit is considered late if it occurs after the yearly due dates. For example, if the last visit occurred on January 1, 2008, the next monitoring visit must occur within 90 days of January 1, 2009.

11. The licensor and licensee or child care staff will complete a compliance agreement to address any violation of WAC or RCW. See “10.1.3 Compliance Agreement” procedure.

The Department of Early Learning Child Care Licensing Policies and Procedures, 10.1.3 Compliance Agreement Procedure, states in part:

Completing the Facility Licensing Compliance Agreement (FLCA)

1. The licensor must use 10.9.1.1 Compliance Agreement form in ELF to record noncompliance issues. If the technology equipment is not working, then the licensor will use the hardcopy 10.9.1.1 Compliance Agreement form.

8. If there is an immediate health and safety issue, the noncompliance issue will be corrected immediately or as soon as possible. Verification of compliance should be completed within 10 business days and follow the process under Compliance Agreement Follow-up section below.

Compliance Agreement Follow-up

1. The licensor must monitor the completion of the compliance agreement.

2. The licensor must verify within 10 business days the correction of licensing noncompliance issues that could impact the health, safety and well-being of children in care. The verification must be documented in FamLink using the health and safety recheck code. Allowable verification is as follows:

a. Health and Safety recheck – An on-site visit is required if the noncompliance issue is a serious health and safety violation which may include but is not limited to:

- i. Health and safety hazards
- ii. Behavior management
- iii. Supervision
- iv. Staff/child interaction
- v. Group size/capacity
- vi. Medication management
- vii. Safe Sleep
- viii. Window blind cords that form a loop

b. Acceptable use of photographic or email verification may include but is not limited to:

- i. Environmental changes
- ii. Indoor/outdoor equipment

3. The licensor must request supervisor approval if they are unable to meet the 10 business day requirement. The supervisor must approve or deny the request and document the decision in FamLink provider notes.

4. If the noncompliance issues do not immediately impact the health, safety, and well-being of children in care, written verification in lieu of a site visit may be used to verify correction of noncompliance. Examples may include but are not limited to:

- a. Menu posting
- b. Documentation of activity program
- c. Supplies verified with receipt
- d. Changes to parent communication
- e. Staff development and training records
- f. Attendance logs
- g. Health Care Plan
- h. Fire Drill record

2018-036

The Department of Social and Health Services did not have adequate internal controls over and did not comply with requirements to detect fraud in the Child Care and Development Fund program.

Federal Awarding Agency: U.S. Department of Health and Human Services
Pass-Through Entity: None
CFDA Number and Title: 93.575 Child Care and Development Block Grant
93.596 Child Care Mandatory and Matching Funds of the Child Care and Development Fund
Federal Award Number: G1801WACCDF; G1701WACCDF; G1601WACCDF
Applicable Compliance Component: Special Test – Fraud Detection and Repayment
Known Questioned Cost Amount: None

Background

The federal Child Care and Development Fund (CCDF) grant helps eligible working families pay for child care. In fiscal year 2018, Washington childcare providers were paid about \$189 million in federal grant funds. Although the Department of Children, Youth and Family (DCYF) (formerly the Department of Early Learning) is the lead agency for the CCDF program, the Department of Social and Health Services' (DSHS) Office of Fraud and Accountability (OFA) has the statutory authority to conduct investigations related to allegations of fraud in the CCDF program. State law requires DCYF to refer suspected incidents of child care subsidy fraud to OFA for appropriate investigation and action.

Both DCYF and DSHS accept reports of suspected fraud online, by mail, phone or fax. Staff from either agency can report suspected fraud through internal systems or to a hotline.

When DSHS receives a report of suspected fraud in a program it oversees, it runs the report through an automated process in its Barcode system to assess the level of potential fraud risk. The process considers which social service programs the client is receiving benefits from, the total benefits (dollars) being received by the client, whether the client has come up on prior reports and the client's overpayment history. These factors are all assigned point values that vary based on the client's particular case. These point values are summed and, based on this total, the suspected fraud is rated from 1 to 5, with 1 being the highest risk level. Once the report is rated, it is received by OFA, which may assign it to an investigator for review. In April 2018, DSHS amended its process to include the amount of CCDF benefits received and the number of children in the home. Previously, this information was not considered by DSHS when assessing risk of suspected fraud reports

OFA supervisors attempt to assign all reports rated as 1 or 2 and then work their way down to lower-rated reports. In February 2018, the OFA Director issued a directive to managers that all reports rated as 1 or 2 should be assigned within 90 days of the case being referred. OFA management explained that some reports are not assigned to investigators because of workload capacity. No matter what priority level is assessed, if a report is not assigned to an investigator within the first 90 days, it is "aged out" and sent back to DSHS program staff. Program staff review the original reported information and decide whether to send the case back through the automated process to be reassessed,

or dismiss the fraud report. In fiscal year 2018, OFA received 2,076 child care fraud reports. Of those, 705 reports (34 percent) aged out of the system.

If an OFA investigation concludes that potential fraud occurred, the results are sent to a local prosecuting attorney's office or United States attorney's office. If a court responds with the legal determination of fraud, the case is forwarded to the Office of Financial Recovery at DSHS, so that an overpayment can be recovered from the client.

In the previous three audits, we reported that DCYF and DSHS lacked adequate internal controls over the identification and detection of child care fraud. The prior finding numbers were 2017-027, 2016-020 and 2015-025.

Description of Condition

We found DSHS did not adequately identify suspected CCDF frauds. DSHS did not update the automated process it used to prioritize fraud reports to include CCDF benefit payments until April 2018 – nine months into the audit period. Before then, the process of assigning point values incorporated only the dollar value of some of the other program benefits, but not CCDF.

The consideration of the CCDF dollar amounts, as well as the number of children in the home, increased the assigned point values, and therefore the risk level of fraud reports for the CCDF program. The increased point value would mean that staff would be required to review these cases.

When comparing the new automated process to the old process, we found 52 of the 80 possible point values (65 percent) for reports scored as level 3 or 4 would have increased to a level 1 or 2 and would therefore be considered a high-priority case for review. This means that for nine months, DSHS was not adequately identifying potential CCDF frauds. Many of the 705 cases that aged out during this period should have been rated as a 1 or 2 and reviewed as high priority cases.

We consider these internal control weaknesses to constitute a material weakness.

Cause of Condition

Reprogramming its automated process took DSHS longer than it expected.

Effect of Condition

By not considering the amount of child care dollars at risk in its automated assessment process for nine months of the year, the Department was at risk of not detecting fraudulent billing activities and not complying with the grant requirement to identify and report CCDF fraud. Non-compliance with grant requirements could potentially disqualify the state from receiving future federal funding.

Recommendation

We recommend DSHS:

- Continue to incorporate child care dollars at risk as a factor when determining the priority of investigating a fraud referral
- Monitor staff to ensure the highest priority level cases (1 and 2) are assigned within 90 days

Department's Response

The Department concurs with the audit finding.

DSHS implemented the fraud scoring system in 2012 using lean techniques. In June 2015, SAO examined the scoring system as part of the Prioritizing Fraud Investigations at the Department of Social and Health Services' Office of Fraud and Accountability performance audit. The SAO audit stated the tool was working as designed, in 2015, to prioritize a workload that was not capable of being worked as a whole, due to the lack of sufficient staffing.

During April 2018, in response to the SFY17 audit, the Department incorporated SAO's recommendations to include child care dollars as a risk factor in determining the priority of fraud referral investigations.

The Department has had a long standing practice of managers assigning cases based off the priority level, starting with the highest priority cases. The Department maintains a goal of completing as many of the highest risk of fraud cases as staffing and workload allows. The Office of Fraud and Accountability (OFA) reports out on this performance measurement monthly and it is reviewed monthly with management.

Additionally, during February 2018, the OFA Senior Director issued a directive to managers that all reports rated as a 1 or 2 should be assigned within 90 days of the case being referred. OFA Managers continue to monitor the monthly status of all FRED cases, included that all cases scored 1 or 2 are assigned out timely.

Auditor's Concluding Remarks

We thank the Department for its cooperation and assistance throughout the audit. We will review the status of the Department's corrective action during our next audit.

Applicable Laws and Regulations

Title 2 U.S. Code of Federal Regulations Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance) establishes the following applicable requirements:

Section 200.303 Internal controls, states in part:

The non-Federal entity must:

- (a) Establish and maintain effective internal control over the Federal award that provides reasonable assurance that the non-Federal entity is managing the Federal award in compliance with Federal statutes, regulations, and the terms and conditions of the Federal award. These internal controls should be in compliance with guidance in “Standards for Internal Control in the Federal Government” issued by the Comptroller General of the United States or the “Internal Control Integrated Framework”, issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).
- (b) Comply with Federal statutes, regulations, and the terms and conditions of the Federal awards.
- (d) Take prompt action when instances of noncompliance are identified including noncompliance identified in audit findings.

Section 200.516 Audit findings, states in part:

- (1) Significant deficiencies and material weaknesses in internal control over major programs and significant instances of abuse relating to major programs. The auditor’s determination of whether a deficiency in internal control is a significant deficiency or material weakness for the purpose of reporting an audit finding is in relation to a type of compliance requirement for a major program identified in the Compliance Supplement.
- (2) Material noncompliance with the provisions of Federal statutes, regulations, or the terms and conditions of Federal awards related to a major program. The auditor’s determination of whether a noncompliance with the provisions of Federal statutes, regulations, or the terms and conditions of Federal awards is material for the purpose of reporting an audit finding is in relation to a type of compliance requirement for a major program identified in the compliance supplement.

The American Institute of Certified Public Accountants defines significant deficiencies and material weaknesses in internal controls over compliance in its *Codification of Statements on Auditing Standards*, section 935, Compliance Audits, as follows:

.11 For purposes of adapting GAAS to a compliance audit, the following terms have the meanings attributed as follows: ...

Deficiency in internal control over compliance. A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance on a timely basis. A deficiency in design exists when (a) a control necessary to meet the control objective is missing, or (b) an existing control is not properly designed so that, even if the control operates as designed, the control objective would not be met. A deficiency in operation exists when a properly designed control does not operate as designed or the person performing the control does not possess the necessary authority or competence to perform the control effectively.

Material weakness in internal control over compliance. A deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a compliance requirement will not be prevented, or detected and corrected, on a timely basis. In this section, a reasonable possibility exists when the likelihood of an event occurring is either reasonably possible or probable as defined as follows:

Reasonably possible. The chance of the future event or events occurring is more than remote but less than likely.

Probable. The future event or events are likely to occur.

Significant deficiency in internal control over compliance. A deficiency, or a combination of deficiencies, in internal control over compliance that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

Material noncompliance. In the absence of a definition of material noncompliance in the governmental audit requirement, a failure to follow compliance requirements or a violation of prohibitions included in the applicable compliance requirements that results in noncompliance that is quantitatively or qualitatively material, either individually or when aggregated with other noncompliance, to the affected government program.

45 Code of Federal Regulations, section 98.60 Availability of funds, states in part:

- (i) Lead Agencies shall recover child care payments that are the result of fraud. These payments shall be recovered from the party responsible for committing the fraud.

Revised Code of Washington 43.216.730 Child care subsidy fraud – Referral – Collection of overpayment, states in part:

- (1) The department must refer all suspected incidents of child care subsidy fraud to the department of social and health services office of fraud and accountability for appropriate investigation and action.
- (2) For the purposes of this section, "fraud" has the definition in RCW 74.04.004.
- (3) This section does not limit or preclude the department or the department of social and health services from establishing and collecting overpayments consistent with federal regulation or seek other remedies that may be legally available, including but not limited to criminal investigation or prosecution

2018-037

The Department of Social and Health Services did not have adequate internal controls over and did not comply with requirements to ensure it separately identified and reported demonstration project costs.

Federal Awarding Agency: Department of Health and Human Services,
Administration for Children and Families

Pass-Through Entity: None

CFDA Number and Title: 93.658 Foster Care – Title IV-E

Federal Award Number: G-1701WAFOST, G-1801WAFOST

Applicable Compliance Component: Reporting
Special Tests and Provisions – Operation of a Foster Care
Demonstration Project

Known Questioned Cost Amount: None

Background

The federal Title IV-E Foster Care program helps states provide safe and stable out-of-home care for children under the jurisdiction of the state’s child welfare agency until the children are returned home, placed with adoptive families or placed in other planned, permanent arrangements. In Washington, the Department of Social and Health Services Children’s Administration (Department) is responsible for overseeing and administering the Foster Care program.

The Department has been operating its IV-E Foster Care program under a demonstration project waiver since January 2014. The waiver allows the Department to waive standard eligibility rules for a specified period and allows federal funds to be used more flexibly to operate projects that test innovative approaches to delivering and financing program services. The goal of the demonstration project is to improve the safety, permanency and well-being of the target population while being cost neutral to the federal awarding agency.

The Department’s approved demonstration project is the Family Assessment Response program (FAR). The purpose of the FAR program is to reduce the number of children placed in foster care by Child Protective Services (CPS). The FAR program accomplishes this by providing an alternative method for CPS to respond to non-emergent allegations of child-neglect. By using federal funds to reduce the need for foster care placement, the Department will, in theory, reduce the cost of operating its traditional foster care system, and thereby accomplish the project goals while not increasing the net cost of the program.

The Department must operate its regular IV-E foster care program in tandem with the demonstration project while the waiver is in effect. The costs for both programs must be separately identified and reported to the federal grantor each quarter based on whether they were standard IV-E foster care program costs or were only allowable because of the demonstration project waiver. This provides the Department and federal grantor some of the data required to determine the effectiveness of the project.

The Department spent about \$125 million in federal grant funds in fiscal year 2018.

As of July 1, 2018, the Legislature created a new state agency that combined the Department's Children's Administration and the Department of Early Learning. The new agency is called the Department of Children, Youth and Families (DCYF) and is now responsible for managing the Foster Care program.

Description of Condition

The Department did not have adequate internal controls over and did not comply with requirements to ensure it separately identified and reported demonstration project costs.

When submitting its quarterly financial reports, the Department did not accurately report the amount it spent on activities that were only allowable with a demonstration project, as required. Instead, the Department reported only those costs that were not allowed to be paid with demonstration funds as traditional foster care spending. All other spending was reported as demonstration project costs. This resulted in the Department improperly reporting a significant amount of traditional foster care costs as demonstration project spending.

We consider this internal control deficiency to be a material weakness.

This condition was not reported in the prior audit.

Cause of Condition

The Department did not have a complete understanding of the requirement for distinct accounting when it began operating under the demonstration project waiver. As a result, the Department designed its accounting system coding to classify costs based on whether they were allowable or unallowable to be paid with demonstration project funds.

Effect of Condition

Because the accounting system does not separately track both cost categories, the Department misreported the amount of expenditures related to the demonstration project to the federal grantor and has likely been doing so since the demonstration project began. Due to this lack of separate accounting, we could not determine how misreported the amounts were.

Recommendation

We recommend the Department:

- Revise its report preparation process and accounting system coding, if necessary, to enable it to separately identify both project cost categories
- Consult with the grantor about whether submitting revised reports from prior years is required

Department's Response

The Department concurs with the finding.

The Department will revise its reporting process in order to accurately identify both categories DCYF has assigned specific Famlink codes for payments and tracking purposes with regard to the Demonstration project.

The Demonstration Project is scheduled to conclude September 30th, 2019.

The Department will work with the grantor if revisions to prior reports are determined to be necessary.

Auditor's Concluding Remarks

We thank the Department for its cooperation and assistance throughout the audit. We will review the status of the Department's corrective action during our next audit.

Applicable Laws and Regulations

Title 2 U.S. Code of Federal Regulations Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance) establishes the following applicable requirements:

Section 200.303 Internal controls, states in part:

The non-Federal entity must:

- (a) Establish and maintain effective internal control over the Federal award that provides reasonable assurance that the non-Federal entity is managing the Federal award in compliance with Federal statutes, regulations, and the terms and conditions of the Federal award. These internal controls should be in compliance with guidance in "Standards for Internal Control in the Federal Government" issued by the Comptroller General of the United States or the "Internal Control Integrated Framework", issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).
- (b) Comply with Federal statutes, regulations, and the terms and conditions of the Federal awards.
- (d) Take prompt action when instances of noncompliance are identified including noncompliance identified in audit findings.

Section 200.516 Audit findings, states in part:

- (a) *Audit findings reported.* The auditor must report the following as audit findings in a schedule of findings and questioned costs:
 - (1) Significant deficiencies and material weaknesses in internal control over major programs and significant instances of abuse relating to major programs. The auditor's determination of whether a deficiency in internal control is a significant deficiency or material weakness for the purpose of reporting an audit finding is in

relation to a type of compliance requirement for a major program identified in the Compliance Supplement.

- (2) Material noncompliance with the provisions of Federal statutes, regulations, or the terms and conditions of Federal awards related to a major program. The auditor's determination of whether a noncompliance with the provisions of Federal statutes, regulations, or the terms and conditions of Federal awards is material for the purpose of reporting an audit finding is in relation to a type of compliance requirement for a major program identified in the compliance supplement.

Title 2 U.S. Code of Federal Regulations Part 200, Appendix XI, Compliance Supplement 2017, Part 3-Compliance Requirements, states in part:

Section N. Special Tests and Provisions, states in part:

2. Operation of a Foster Care Demonstration Project (Applicable Only for Title IV-E Agencies with ACF Approval to Operate a Foster Care Demonstration Project)

Compliance Requirement – Those Title IV-E agencies that receive approval to operate a foster care demonstration project for a specified period of time must do so in accordance with ACF-approved terms and conditions that define the operational parameters and the waivers granted. The funding for operation of such a project is subject to a cost neutrality limit that is calculated either through an experimental design (involving experimental group cases and either a control or matched comparison group process) or an established capped allocation table for identified populations (including agency-wide) in specific funding categories.

All Title IV-E agencies that operate a foster care demonstration project are also simultaneously continuing to operate the traditional (non-demonstration) foster care program for some portion of the agency's service population and/or funding categories. Operation of a foster care demonstration project, therefore, includes both the continuation of assistance payments and, where applicable, administration or training under the existing approved Title IV-E Plan and provision of project interventions or other waiver-based services for an identified population. Demonstration project operational costs, to the extent that they provide payments, administration or training that is allowable for traditional Title IV-E foster care funding, must be in compliance with all applicable Title IV-E requirements (unless waived) and are subject to separate identification as part of financial reporting. Funding is also available, subject to separate ACF approvals, for the costs of demonstration project developmental and evaluation costs.

The American Institute of Certified Public Accountants defines significant deficiencies and material weaknesses in internal controls over compliance in its *Codification of Statements on Auditing Standards*, section 935, Compliance Audits, as follows:

.11 For purposes of adapting GAAS to a compliance audit, the following terms have the meanings attributed as follows: ...

Deficiency in internal control over compliance. A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance on a timely basis. A deficiency in design exists when (a) a control necessary to meet the control objective is missing, or (b) an existing control is not properly designed so that, even if the control operates as designed, the control objective would not be met. A deficiency in operation exists when a properly designed control does not operate as designed or the person performing the control does not possess the necessary authority or competence to perform the control effectively.

Material weakness in internal control over compliance. A deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a compliance requirement will not be prevented, or detected and corrected, on a timely basis. In this section, a reasonable possibility exists when the likelihood of an event occurring is either reasonably possible or probable as defined as follows:

Reasonably possible. The chance of the future event or events occurring is more than remote but less than likely.

Probable. The future event or events are likely to occur.

Significant deficiency in internal control over compliance. A deficiency, or a combination of deficiencies, in internal control over compliance that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

Material noncompliance. In the absence of a definition of material noncompliance in the governmental audit requirement, a failure to follow compliance requirements or a violation of prohibitions included in the applicable compliance requirements that results in noncompliance that is quantitatively or qualitatively material, either individually or when aggregated with other noncompliance, to the affected government program.

2018-038 The Department of Social and Health Services improperly charged \$798,930 to the federal foster care grant.

Federal Awarding Agency: Department of Health and Human Services, Administration for Children and Families
Pass-Through Entity: None
CFDA Number and Title: 93.658 Foster Care – Title IV-E
Federal Award Number: G-1701WAFOST, G-1801WAFOST
Applicable Compliance Component: Activities Allowed or Unallowed, Allowable Costs/Cost Principles
Known Questioned Cost Amount: \$798,930

Background

The federal Title IV-E Foster Care program helps states provide safe and stable out-of-home care for children under the jurisdiction of the State’s child welfare agency until the children are returned home, placed with adoptive families or placed in other planned, permanent arrangements. The program provides funds to reduce the costs of foster care for eligible children, reduce administrative costs to manage the program, and provide training for adults in the Foster Care program, including state agency staff, foster parents and certain private agency staff. In Washington, the Department of Social and Health Services Children’s Administration (Department) is responsible for overseeing and administering the Foster Care program.

The Department is responsible for ensuring grant money is used only for costs allowable under the grant and that payments are adequately supported. During fiscal year 2018, the Department spent about \$125 million in federal grant funds, with over \$32 million paid to foster care service providers.

As of July 1, 2018, the Legislature created a new state agency that combined the Department’s Children’s Administration and the Department of Early Learning. The new agency is called the Department of Children, Youth and Families (DCYF) and is now responsible for managing the Foster Care program.

In the prior audit, we reported the Department improperly charged costs to the grant. The prior finding number was 2017-028.

Description of Condition

The Department of Social and Health Services improperly charged \$798,930 to the federal foster care grant.

As part of the audit, we attempted to reconcile the Department’s payment data with its accounting records to ensure our testing population was complete. The accounting records showed the Department paid \$32,805,946 in federal funds to providers. However, according to the Department’s provider payment system, it spent only \$32,008,206 for these services. During the audit, the Department

attempted to reconcile the data sets to determine what caused the difference, but was unable to do so. We therefore determined \$797,740 of the recorded federal expenditures was not supported.

We used a statistical sampling method to randomly select and examine 59 foster care provider payments from a total population of 120,670 payments, and identified two exceptions.

The first payment in question was a provider payment paid on behalf of a foster child who was determined to need behavioral rehabilitation services (BRS). These services can vary and the Department authorized the child for a high level of services, but did not document the rate at which the provider was to be paid or how that rate was supported. Because the child was eligible for BRS, and therefore entitled to at least the most basic BRS amount, we subtracted the lowest monthly BRS rate from the rate the Department paid and are questioning the rest of the payment. This resulted in known questioned costs of \$1,078.

The second payment in question was made to a vendor for visitation services. The authorization for these services expired three months prior to the services being provided. This resulted in known questioned cost of \$111.

Federal regulations require the auditor to issue a finding when the known or estimated questioned costs identified in a single audit exceed \$25,000. We are issuing this finding because, as stated in the Effect of Condition and Questioned Costs section of this finding, the estimated questioned costs exceed that threshold.

Cause of Condition

The Department said the difference between the accounting record and the payment system resulted from multiple factors. These factors include contract payments made outside of the provider payment system, payment adjustments in its case management system and journal voucher adjustments. However, the Department could not provide documentation to adequately support any of the variance.

The Department did not have any policies or procedures in place to ensure that BRS rates were adequately documented or those vendor billings for visitation services were adequately reviewed to ensure they were allowable.

Effect of Condition and Questioned Costs

A statistical sampling method was used to randomly select the 59 payments examined in the audit. We found \$1,190 of improper federal payments. We estimate the amount of likely improper federal payments to be \$689,552. The federal payments were matched by state payments, and we found \$1,190 of improper state payments as well; we estimate the likely improper state payments to also be \$689,552. The amount of likely improper state payments is not included in the federal questioned costs.

We question costs when we find an agency has not complied with grant regulations or when it does not have adequate documentation to support its expenditures.

Our sampling methodology meets statistical sampling criteria under generally accepted auditing standards in AU-C 530.05. It is important to note that the sampling technique we used is intended to

support our audit conclusions by determining if expenditures complied with program requirements in all material respects. Accordingly, we used an acceptance sampling formula designed to provide a high level of assurance, with a 95 percent confidence of whether exceptions exceeded our materiality threshold. Our audit report and finding reflects this conclusion. However, the likely improper payment projections are a point estimate and only represent our “best estimate of total questioned costs” as required by 2 CFR 200.516(3). To ensure a representative sample, we stratified the population by dollar amount.

Recommendations

We recommend the Department:

- Ensure only expenditures supported by the Department’s accounting records are charged to the grant
- Ensure charges have been authorized and are adequately supported before paying
- Consult with the grantor to discuss whether the questioned costs identified in the audit should be repaid

Department’s Response

The Department partially concurs with the finding.

We concur the support for one client’s BRS rate was not documented and the service referral for one child to one vendor was expired.

We do not concur that \$797,740 of federal expenditures were not supported.

Not all foster care payments are located in SSPS. AFRS is the state’s accounting system of record. While AFRS does interface with SSPS, there will always be a difference in the total expenditures, given SSPS is not the only payment mechanism utilized when paying for services.

The Title IV-E difference in expenditures between SSPS and AFRS is the result of multiple factors. These expenditures are paid outside of SSPS, but are recorded in AFRS. These expenditures include:

- *Contractor payments*
- *Updates to SSPS and Famlink*
- *A-19 payments*
- *Recoveries received*
- *Adjustments needed to appropriately claim Title IV-E dollars*

The Department will work with the Department of Health and Human Service if they determine question costs should be repaid.

Auditor’s Concluding Remarks

We worked with the Department for more than five months attempting to reconcile the amounts expended and obtain the support for the expenditures. This included requesting any and all

documentation, from any source the Department had to support them. The Department did not provide adequate supporting documentation for the \$797,740 in question.

We reaffirm our finding and will review the status of the Department's corrective action during our next audit.

Applicable Laws and Regulations

Title 2 U.S. Code of Federal Regulations Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance) establishes the following applicable requirements:

Section 200.53 Improper Payments states:

- (a) *Improper payment* means any payment that should not have been made or that was made in an incorrect amount (including overpayments and underpayments) under statutory, contractual, administrative, or other legally applicable requirements; and
- (b) *Improper payment* includes any payment to an ineligible party, any payment for an ineligible good or service, any duplicate payment, any payment for a good or service not received (except for such payments where authorized by law), any payment that does not account for credit for applicable discounts, and any payment where insufficient or lack of documentation prevents a reviewer from discerning whether a payment was proper.

Section 200.403 Factors affecting Allowability of costs.

Except where otherwise authorized by statute, costs must meet the following general criteria in order to be allowable under Federal awards.

- (a) Be necessary and reasonable for the performance of the Federal award and be allocable thereto under these principles.
- (b) Conform to any limitations or exclusions set forth in these principles or in the Federal award as to types or amount of cost items.
- (c) Be consistent with policies and procedures that apply uniformly to both federally-financed and other activities of the non-Federal entity.
- (d) Be accorded consistent treatment. A cost may not be assigned to a Federal award as a direct cost if any other cost incurred for the same purpose in like circumstances has been allocated to the Federal award as an indirect cost.
- (e) Be determined in accordance with generally accepted accounting principles (GAAP), except, for state and local governments and Indian tribes only, as otherwise provided for in this part.
- (f) Not be included as a cost or used to meet cost sharing or matching requirements of any other federally-financed program in either the current or a prior period. See also §200.306 Cost sharing or matching paragraph (b).
- (g) Be adequately documented. See also §§200.300 Statutory and national policy requirements through 200.309 Period of performance of this part.

Section 200.410 Collection of unallowable costs.

Payments made for costs determined to be unallowable by either the Federal awarding agency, cognizant agency for indirect costs, or pass-through entity, either as direct or indirect costs, must be refunded (including interest) to the Federal Government in accordance with instructions from the Federal agency that determined the costs are unallowable unless Federal statute or regulation directs otherwise. See also Subpart D—Post Federal Award Requirements of this part, §§200.300 Statutory and national policy requirements through 200.309 Period of performance.

Section 200.516 Audit findings, states in part:

(a) *Audit findings reported.* The auditor must report the following as audit findings in a schedule of findings and questioned costs:

(3) Known questioned costs that are greater than \$25,000 for a type of compliance requirement for a major program. Known questioned costs are those specifically identified by the auditor. In evaluating the effect of questioned costs on the opinion on compliance, the auditor considers the best estimate of total costs questioned (likely questioned costs), not just the questioned costs specifically identified (known questioned costs). The auditor must also report known questioned costs when likely questioned costs are greater than \$25,000 for a type of compliance requirement for a major program. In reporting questioned costs, the auditor must include information to provide proper perspective for judging the prevalence and consequences of the questioned costs.

2018-039

The Department of Social and Health Services did not have adequate internal controls over and did not comply with federal level of effort requirements for the Adoption Assistance program.

Federal Awarding Agency: U.S. Department of Health and Human Services
Pass-Through Entity: None
CFDA Number and Title: 93.659 Adoption Assistance- Title IV-E
Federal Award Number: G-1701WAADPT; G-1801WAADPT
Applicable Compliance Component: Level of Effort
Known Questioned Cost Amount: None

Background

The Department of Social and Health Services' (Department) Children's Administration operates the Adoption Assistance program to provide funding for parents who adopt eligible children with special needs. The program provides financial and medical benefits to qualified children. Adoptive parents can receive a monthly assistance payment from the Department to care for the children, in addition to expenses related to the initial placement of the child in the home such as court fees, payments for medical visits and transportation costs.

The Department spent almost \$50 million on Adoption Assistance in fiscal year 2018, with more than \$40 million paid to the adoptive parents of eligible children for adoption services.

In October 2010, the federal government implemented a new set of eligibility requirements designed to be less restrictive. These new requirements allowed states to save money by claiming federal reimbursement on previously unallowable services.

In conjunction with the new eligibility requirements came a new regulation that required the states to:

- Calculate the amount saved, if any
- Spend those savings on social services outlined under titles IV-B or IV-E of the Social Security Act, while ensuring they spent no less than 30 percent of any such savings on post-adoption services, post-guardianship services, and services to support and sustain positive permanent outcomes for children who might otherwise enter the State foster care program. At least two-thirds of that amount must be spent on post-adoption and post-guardianship services. Maintaining this state-spending at the appropriate level is referred to as level of effort.
- Accurately report savings and expenditures to the grantor

In the previous two audits, we reported the Department did not have adequate internal controls over and did not comply with federal level-of-effort requirements for the Adoption Assistance program. The prior finding numbers were 2017-030 and 2016-026.

As of July 1, 2018, the Legislature created a new state agency that combined the Department's Children's Administration and the Department of Early Learning. The new agency is called the

Department of Children, Youth and Families (DCYF) and is now responsible for managing the Adoption Assistance program.

Description of Condition

The Department did not have adequate internal controls over and did not comply with federal level-of-effort requirements. Specifically, the Department misreported its adoption-savings expenditures to the federal grantor.

Using accounting records, we verified the Department's adoption savings during the audit period was \$1,036,200. Instead of reporting the amount of the savings that was actually spent, the Department reported \$310,860, which was its adoption savings multiplied by 30 percent. We asked the Department to provide records showing the actual amount of adoption savings it spent that should have been reported, but no records were provided.

We consider these internal control weaknesses to constitute a material weakness

Cause of Condition

The adoption savings expenditure figure was misreported because the preparer of the level-of-effort report did not understand the reporting requirement and the Department's review did not detect the error before submission.

Additionally, the Department did not establish written policies and procedures instructing staff on how to identify and report adoption saving expenditures.

Effect of Condition

Because the Department did not comply with the federal level-of-effort requirement, the grantor did not receive accurate information about the Adoption Support program.

Recommendations

We recommend the Department:

- Establish written policies and procedures specifying how to identify and report adoption savings expenditures
- Review level-of-effort reports to ensure the expenditures reported to the grantor have been accurately determined and are adequately supported

Department's Response

The Children's Administration concurs with the finding.

We will establish written procedures for staff to identify and accurately report adoption savings expenditures. The written procedures will include quarterly reports to ensure adequate support for reported expenditures.

Auditor's Concluding Remarks

We thank the Department for its cooperation and assistance throughout the audit. We will review the status of the Department's corrective action during our next audit.

Applicable Laws and Regulations

Title 2 U.S. Code of Federal Regulations Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance) establishes the following applicable requirements:

Section 200.303 Internal controls, states in part:

The non-Federal entity must:

- (a) Establish and maintain effective internal control over the Federal award that provides reasonable assurance that the non-Federal entity is managing the Federal award in compliance with Federal statutes, regulations, and the terms and conditions of the Federal award. These internal controls should be in compliance with guidance in "Standards for Internal Control in the Federal Government" issued by the Comptroller General of the United States or the "Internal Control Integrated Framework", issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).
- (b) Comply with Federal statutes, regulations, and the terms and conditions of the Federal awards.
- (d) Take prompt action when instances of noncompliance are identified including noncompliance identified in audit findings.

Section 200.516 Audit findings, states in part:

- (a) *Audit findings reported.* The auditor must report the following as audit findings in a schedule of findings and questioned costs:
 - (1) Significant deficiencies and material weaknesses in internal control over major programs and significant instances of abuse relating to major programs. The auditor's determination of whether a deficiency in internal control is a significant deficiency or material weakness for the purpose of reporting an audit finding is in relation to a type of compliance requirement for a major program identified in the Compliance Supplement.
 - (2) Material noncompliance with the provisions of Federal statutes, regulations, or the terms and conditions of Federal awards related to a major program. The auditor's determination of whether a noncompliance with the provisions of Federal statutes, regulations, or the terms and conditions of Federal awards is material for the purpose

of reporting an audit finding is in relation to a type of compliance requirement for a major program identified in the compliance supplement.

The American Institute of Certified Public Accountants defines significant deficiencies and material weaknesses in internal controls over compliance in its *Codification of Statements on Auditing Standards*, section 935, Compliance Audits, as follows:

.11 For purposes of adapting GAAS to a compliance audit, the following terms have the meanings attributed as follows: ...

Deficiency in internal control over compliance. A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance on a timely basis. A deficiency in design exists when (a) a control necessary to meet the control objective is missing, or (b) an existing control is not properly designed so that, even if the control operates as designed, the control objective would not be met. A deficiency in operation exists when a properly designed control does not operate as designed or the person performing the control does not possess the necessary authority or competence to perform the control effectively.

Material weakness in internal control over compliance. A deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a compliance requirement will not be prevented, or detected and corrected, on a timely basis. In this section, a reasonable possibility exists when the likelihood of an event occurring is either reasonably possible or probable as defined as follows:

Reasonably possible. The chance of the future event or events occurring is more than remote but less than likely.

Probable. The future event or events are likely to occur.

Significant deficiency in internal control over compliance. A deficiency, or a combination of deficiencies, in internal control over compliance that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

Material noncompliance. In the absence of a definition of material noncompliance in the governmental audit requirement, a failure to follow compliance requirements or a violation of prohibitions included in the applicable compliance requirements that results in noncompliance that is quantitatively or qualitatively material, either individually or when aggregated with other noncompliance, to the affected government program.

42 U.S. Code § 673 – Adoption and guardianship assistance program states, in part:

- (a) Agreements with Adoptive Parents of Children with Special Needs; State Payments; Qualifying Children; Amount of Payments; Changes in Circumstances; Placement Period Prior to Adoption; Nonrecurring Adoption Expenses
 - (8)
 - (A) A State shall calculate the savings (if any) resulting from the application of paragraph (2)(A)(ii) to all applicable children for a fiscal year, using a methodology specified by the Secretary or an alternate methodology proposed by the State and approved by the Secretary.
 - (B) A State shall annually report to the Secretary—
 - (i) the methodology used to make the calculation described in subparagraph (A), without regard to whether any savings are found;
 - (ii) the amount of any savings referred to in subparagraph (A); and
 - (iii) how any such savings are spent, accounting for and reporting the spending separately from any other spending reported to the Secretary under part B or this part.
 - (C) The Secretary shall make all information reported pursuant to subparagraph (B) available on the website of the Department of Health and Human Services in a location easily accessible to the public.
 - (D)
 - (i) A State shall spend an amount equal to the amount of the savings (if any) in State expenditures under this part resulting from the application of paragraph (2)(A)(ii) to all applicable children for a fiscal year, to provide to children of families any service that may be provided under part B or this part. A State shall spend not less than 30 percent of any such savings on post-adoption services, post-guardianship services, and services to support and sustain positive permanent outcomes for children who otherwise might enter into foster care under the responsibility of the State, with at least $\frac{2}{3}$ of the spending by the State to comply with such 30 percent requirement being spent on post-adoption and post-guardianship services.
 - (ii) Any State spending required under clause (i) shall be used to supplement, and not supplant, any Federal or non-Federal funds used to provide any service under part B or this part.

2018-040

The Department of Health did not have adequate internal controls to ensure it complied with survey requirements for Medicaid hospitals and home health agencies.

Federal Awarding Agency: U.S. Department of Health and Human Services
Pass-Through Entity: None
CFDA Number and Title: 93.775 State Medicaid Fraud Control Units
93.777 State Survey and Certification of Health Care Providers and Suppliers (Title XVIII) Medicare
93.778 Medical Assistance Program (Medicaid; Title XIX)
Federal Award Number: 1805WA5MAP; 1805WA5ADM; 1805WAIMPL; 1805WAINCT
Applicable Compliance Component: Special Tests and Provisions – Provider Health and Safety Standards
Known Questioned Cost Amount: None

Background

Medicaid is a jointly funded state and federal partnership providing coverage for about 1.9 million eligible low-income Washington residents who otherwise might go without medical care. Medicaid is Washington’s largest public assistance program and accounts for about one-third of the State’s federal expenditures. The program spent about \$12.7 billion in federal and state funds during fiscal year 2018.

The state Medicaid program spent about \$17.3 million to certify health care providers, including hospitals, home health agencies, intermediate care facilities and nursing facilities in fiscal year 2018. Of this amount, the Department of Health (Department) spent about \$1.8 million certifying acute care, critical access and psychiatric hospitals, as well as home health agencies. The State had 39 hospitals and 60 home health agencies that were Medicare and/or Medicaid certified.

The Department is responsible for certifying and surveying all hospitals and home health agencies with a non-deemed status, meaning the facilities are not subject to certification from an outside accrediting organization. Instead, the Department performs surveys to ensure the facilities meet minimum health and safety requirements and communicates the results to the Centers for Medicare and Medicaid Services.

The survey for certifying a facility is a patient-centered inspection that gathers information about the quality of service furnished in a facility to determine compliance with the requirements for participation. The survey focuses on the facility’s administration and patient services. The survey also assesses compliance with federal health, safety and quality standards designed to ensure patients receive safe and quality care services.

Federal law requires home health agencies to receive a federal certification survey at least every 36 months, while the minimum federal requirement for hospitals is every 60 months. In addition, federal rule requires that if a survey uncovers deficiencies, the Department must mail a Statement of Deficiency to the facility within 10 working days of the survey exit date. The facility must then submit a Plan of Correction that the Department determines is acceptable within 60 calendar days of receipt, or risk forfeiting its Medicaid certification.

Description of Condition

The Department did not have adequate internal controls to ensure it complied with survey requirements for Medicaid hospitals and home health agencies.

We examined survey documentation for all 18 hospital certification surveys and 15 home health agency certification surveys completed during the audit period. We found two instances (6 percent) when the Department did not mail Statements of Deficiencies within 10 working days as required. One of these cases was a hospital survey, and the second was a home health agency survey.

We consider this internal control deficiency to be a material weakness.

This condition was not reported in the prior audit.

Cause of Condition

The Department uses the Integrated Licensing Reporting System (ILRS) to track Statements of Deficiency from draft to final submission, as well as the status of hospital and home health agency Plans of Correction. Survey management did not closely monitor the activity within this system to identify the surveys with Statements of Deficiencies taking more than 10 working days to finalize and submit to the facilities. In addition, the ILRS system does not alert management when 10 working days have passed before a Statement of Deficiencies is sent to the facility.

Effect of Condition

While the Department communicates preliminary deficiencies to both hospitals and home health agencies during an exit conference at the conclusion of the onsite survey, when the Department does not send Statements of Deficiencies within 10 working days as required by CMS, the facility does not receive their formal statement of deficiencies and this may delay the development and submission of an acceptable Plan of Correction. In the event the Department is required to follow up on the deficiencies, this may delay the process.

Recommendation

We recommend the Department strengthen internal controls to ensure Statements of Deficiencies are submitted within 10 working days after completing the initial survey.

Department's Response

Thank you for making us aware of this issue. We concur with the recommendations.

As a standard practice, and a general policy of CMS, the Department provides an overview of the deficiencies during an "exit conference" at the conclusion of the onsite survey. The purpose of the exit conference is to informally communicate preliminary survey team findings and provide an opportunity for the interchange of information, especially if there are differences of opinion. It informs the facility of any issues prior to receiving the SOD and helps to promote timely remediation of quality of care or safety problems.

One of the surveys completed was an out of the ordinary survey where it was necessary to correspond back and forth with CMS in the completion of the survey that resulted in an unintended delay in issuing the statement of deficiencies (SOD). We did not obtain written verification from CMS confirming the late issuance of the SOD. In the future, we will ensure we obtain written verification when we anticipate that a SOD may be issued late.

Auditor's Concluding Remarks

We thank the Department for its cooperation and assistance throughout the audit. We will review the status of the Department's corrective action during our next audit.

Applicable Laws and Regulations

Title 2 U.S. Code of Federal Regulations Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance) establishes the following applicable requirements:

Section 200.303 Internal controls, states in part:

The non-Federal entity must:

- (a) Establish and maintain effective internal control over the Federal award that provides reasonable assurance that the non-Federal entity is managing the Federal award in compliance with Federal statutes, regulations, and the terms and conditions of the Federal award. These internal controls should be in compliance with guidance in "Standards for Internal Control in the Federal Government" issued by the Comptroller General of the United States or the "Internal Control Integrated Framework", issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).

Section 200.516 Audit findings, states in part:

- (a) *Audit findings reported.* The auditor must report the following as audit findings in a schedule of findings and questioned costs:
 - (1) Significant deficiencies and material weaknesses in internal control over major programs and significant instances of abuse relating to major programs. The auditor's determination of whether a deficiency in internal control is a significant deficiency or material weakness for the purpose of reporting an audit finding is in

relation to a type of compliance requirement for a major program identified in the Compliance Supplement.

The American Institute of Certified Public Accountants defines significant deficiencies and material weaknesses in internal controls over compliance in its *Codification of Statements on Auditing Standards*, section 935, Compliance Audits, as follows:

.11 For purposes of adapting GAAS to a compliance audit, the following terms have the meanings attributed as follows: ...

Deficiency in internal control over compliance. A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance on a timely basis. A deficiency in design exists when (a) a control necessary to meet the control objective is missing, or (b) an existing control is not properly designed so that, even if the control operates as designed, the control objective would not be met. A deficiency in operation exists when a properly designed control does not operate as designed or the person performing the control does not possess the necessary authority or competence to perform the control effectively.

Material weakness in internal control over compliance. A deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a compliance requirement will not be prevented, or detected and corrected, on a timely basis. In this section, a reasonable possibility exists when the likelihood of an event occurring is either reasonably possible or probable as defined as follows:

Reasonably possible. The chance of the future event or events occurring is more than remote but less than likely.

Probable. The future event or events are likely to occur.

Significant deficiency in internal control over compliance. A deficiency, or a combination of deficiencies, in internal control over compliance that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

Centers for Medicare and Medicaid Services, State Operations Manual, Chapter 2 – The Certification Process, states in part:

2728 – Statement of Deficiencies and Plan of Correction, Form CMS-2567

The SA mails the provider/supplier a copy of Form CMS-2567 within 10 working days after the survey. If there are deficiencies, the SA allows the provider/supplier 10 calendar days to complete and return the PoC.

2018-041 The Health Care Authority did not have adequate internal controls over and did not comply with a state law requirement to perform semi-annual data sharing with health insurers.

Federal Awarding Agency: U.S. Department of Health and Human Services
Pass-Through Entity: None
CFDA Number and Title: 93.775 State Medicaid Fraud Control Units
93.777 State Survey and Certification of Health Care Providers and Suppliers (Title XVIII) Medicare
93.778 Medical Assistance Program (Medicaid; Title XIX)
Federal Award Number: 1805WA5MAP; 1805WA5ADM; 1805WAIMPL; 1805WAINCT
Applicable Compliance Component: Allowable Costs/Cost Principles
Questioned Cost Amount: None

Background

Medicaid is a jointly funded state and federal partnership providing coverage for about 1.9 million eligible low-income Washington residents who otherwise might go without medical care. Medicaid is Washington’s largest public assistance program and accounts for about one-third of the State’s federal expenditures. The program spent about \$13.2 billion in federal and State funds during fiscal year 2018.

It is common for Medicaid beneficiaries to have one or more additional sources of coverage for healthcare services. Third-party liability refers to the legal obligation of third parties, such as insurance companies, to pay part or all of the expenditures for medical assistance furnished under a Medicaid state plan. By law, Medicaid is the “payer of last resort,” meaning all other available third-party resources must meet their legal obligation to pay claims before the Medicaid program pays for the care of an individual eligible for Medicaid.

The federal Deficit Reduction Act of 2005 (Act) requires health insurers to give states eligibility and coverage information that will enable Medicaid agencies to determine whether clients have third-party coverage. As a condition of receiving federal Medicaid funding, the Act directed states to enact laws requiring health insurers doing business in their state to provide the eligibility and coverage information necessary to determine whether Medicaid clients have third-party coverage.

To comply with this requirement, in 2007 the Legislature passed Revised Code of Washington (RCW) 74.09A, which requires the Health Care Authority (Authority) to provide Medicaid client eligibility and coverage information to health insurers. As a condition of doing business with the state, the insurers must use that information to identify Medicaid clients with third-party coverage and provide those results to the Authority. The law requires the exchange of data to occur at least twice a year. The Authority must focus its implementation of the law on those health insurers with the highest probability of joint beneficiaries.

In January 2015, the U.S. Government Accountability Office (GAO) published audit report GAO-15-208, *Additional Federal Action Needed to Further Improve Third-Party Liability Efforts* for the Medicaid program. GAO also found states commonly face challenges with their third-party liability efforts, such as health insurers refusing the provider coverage information or denying liability for procedural reasons.

Since 2008, we have reported findings regarding lack of internal controls over and noncompliance with state law. Prior audit finding numbers were 2017-031, 2016-028, 2015-030, 2014-034, 2013-020, 12-49, 11-38, 10-40, 09-19 and 08-25.

Description of Condition

The Authority did not have adequate internal controls over and did not comply with a state law requirement to perform semi-annual data sharing with health insurers.

The Centers for Medicare and Medicaid Services developed the Payer Initiated Eligibility/Benefits (PIE) transaction, the format was developed by the federal government for data sharing. The Authority implemented this transaction format in July 2013. In October 2013, the Authority sent letters to 10 major insurance carriers with the most Medicaid clients, inviting them to begin data sharing. Three carriers – Regence, Bridgespan and Assuris – have chosen to work with the Authority to implement the PIE transaction and share data.

During fiscal year 2018, the Authority refined the logic for uploading PIE data files into its Medicaid Management Information System, ProviderOne, to ensure accurate automated loading of data. However, the Authority could not complete data exchanges because of data file uploading issues. The Authority worked with the ProviderOne vendor and resolved the issues on June 1, 2018. The file uploading process re-commenced the first week of July 2018, outside of the audit period.

Also, state law (74.09A.020(1)) stipulates that the Authority is to provide client data to health insurers, and the insurers are to identify joint beneficiaries and transmit the information to the Authority. The law and the Authority's current practice do not align because this identification is not being done by the insurers. In practice, the data exchange is initiated by payers (insurers) and then the Authority uploads primary payer information into ProviderOne. .

Cause of Condition

The Authority asserts it has no legal influence to enforce or compel private insurance carriers to participate in the PIE data exchange.

The Authority could not complete all data exchanges because of system upload issues.

Effect of Condition

Without performing the data exchange and cross-matching insurance claims, the Authority cannot completely and promptly identify Medicaid clients who have third-party coverage. This increases the Authority's risk of paying claims that are not allowable.

Because this finding reports non-compliance with state law, the Office of Financial Management is required (RCW 43.09.312(1)) to submit the agency's response and plan for remediation to the Governor, the Joint Legislative Audit and Review Committee and the relevant fiscal and policy committees of the Senate and House of Representatives.

Recommendations

We recommend the Authority:

- Work with the Legislature to bring Washington into compliance with state law
- Continue efforts to perform data matches with private insurers

Authority's Response

The SAO is correct in stating that not all health insurers participate semi-annual data sharing processes with the Health Care Authority (HCA) according to the specifics described in state law (RCW 74.09A.020(5)). The SAO is not correct in concluding that, because of this, HCA is not able to promptly identify Medicaid clients with third party insurance coverage.

Insurers do share data, and HCA has robust and effective processes for identifying and collecting from third parties, much of which happens on an on-going basis and in real time. These activities include data exchanges with insurers; data matching using information obtained from other governmental agencies; cross-matching of insurance claims; and regularly exchanging data with our Medicaid Managed Care Organizations (MCOs). Acting on behalf of HCA, as required by contract, MCOs perform data matches with insurance carriers in the State of Washington that includes the utilization of large national databases to identify third party coverage. MCOs regularly share the results of their data matches with HCA. HCA has found these activities to be very effective in the timely identification of third party insurers.

SAO's finding is based on a specific data exchange method which most carriers have chosen not to participate in and which HCA has no legal authority to enforce. SAO management stated it believes HCA should seek and obtain that legal authority through legislation, and continues this audit finding in support of that opinion. The Office of the Insurance Commissioner is responsible for regulating insurers, not HCA. HCA has requested legislation to amend the specific details of data exchange to align with the data exchange method used by HCA. This legislation will not give HCA enforcement authority to require insurers to participate in that specific data exchange.

HCA will continue to engage in a variety of effective third party liability identification activities, including encouraging insurance carriers to share data, as we have been doing for many years.

Auditor’s Concluding Remarks

State law (RCW 74.09A) requires the Authority to use a specific method of data exchange to accomplish third-party verification. The Authority is not using that method, putting it out of material compliance with the law.

The Authority does engage in other methods of third-party payment verification. However, the Authority will continue to be bound by the specific requirements of state law, just as our Office is bound by the requirement to audit to that standard. Because a state law is at issue, our Office suggested the Authority work with the Legislature on a resolution.

We reaffirm our finding and will review the status of this issue during our next audit.

Applicable Laws and Regulations

Title 2 U.S. Code of Federal Regulations Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance) establishes reporting requirements for audit findings.

Section 200.303 Internal controls.

The non-Federal entity must:

- (a) Establish and maintain effective internal control over the Federal award that provides reasonable assurance that the non-Federal entity is managing the Federal award in compliance with Federal statutes, regulations, and the terms and conditions of the Federal award. These internal controls should be in compliance with guidance in “Standards for Internal Control in the Federal Government” issued by the Comptroller General of the United States or the “Internal Control Integrated Framework”, issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).
- (b) Comply with Federal statutes, regulations, and the terms and conditions of the Federal awards.

Section 200.516 Audit reporting, states in part:

- (a) *Audit findings reported.* The auditor must report the following as audit findings in a schedule of findings and questioned costs:
 - (1) Significant deficiencies and material weaknesses in internal control over major programs and significant instances of abuse relating to major programs. The auditor’s determination of whether a deficiency in internal control is a significant deficiency or material weakness for the purpose of reporting an audit finding is in relation to a type of compliance requirement for a major program identified in the Compliance Supplement.
 - (2) Material noncompliance with the provisions of Federal statutes, regulations, or the terms and conditions of Federal awards related to a major program. The auditor’s determination of whether a noncompliance with the provisions of Federal statutes, regulations, or the terms and conditions of Federal awards is material for the purpose of reporting an audit finding is in relation to a type of compliance requirement for a major program identified in the compliance supplement.

The American Institute of Certified Public Accountants defines significant deficiencies and material weaknesses in internal controls over compliance in its *Codification of Statements on Auditing Standards*, section 935, Compliance Audits:

.11 For purposes of adapting GAAS to a compliance audit, the following terms have the meanings attributed as follows: ...

Deficiency in internal control over compliance. A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance on a timely basis. A deficiency in design exists when (a) a control necessary to meet the control objective is missing, or (b) an existing control is not properly designed so that, even if the control operates as designed, the control objective would not be met. A deficiency in operation exists when a properly designed control does not operate as designed or the person performing the control does not possess the necessary authority or competence to perform the control effectively.

Material weakness in internal control over compliance. A deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a compliance requirement will not be prevented, or detected and corrected, on a timely basis. In this section, a reasonable possibility exists when the likelihood of an event occurring is either reasonably possible or probable as defined as follows:

Reasonably possible. The chance of the future event or events occurring is more than remote but less than likely.

Probable. The future event or events are likely to occur.

Significant deficiency in internal control over compliance. A deficiency, or a combination of deficiencies, in internal control over compliance that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

Material noncompliance. In the absence of a definition of material noncompliance in the governmental audit requirement, a failure to follow compliance requirements or a violation of prohibitions included in the applicable compliance requirements that results in noncompliance that is quantitatively or qualitatively material, either individually or when aggregated with other noncompliance, to the affected government program.

Title 42, United States Code, Part 1396a(a)(25) State plan for medical assistance, states in part:

(A) that the State or local agency administering such plan will take all reasonable measures to ascertain the legal liability of third parties (including health insurers, self-insured plans, group health plans (as defined in section 607(1) of the Employee Retirement Income Security Act of 1974 [[29 U.S.C. 1167\(1\)](#)]), service benefit plans, managed care organizations, pharmacy benefit managers, or other parties that are, by statute, contract, or agreement, legally responsible for payment of a claim for a health care item or service) to pay for care and services available under the plan, including-

(i) the collection of sufficient information (as specified by the Secretary in regulations) to enable the State to pursue claims against such third parties, with such information being

collected at the time of any determination or redetermination of eligibility for medical assistance, and

- (ii) the submission to the Secretary of a plan (subject to approval by the Secretary) for pursuing claims against such third parties, which plan shall be integrated with, and be monitored as a part of the Secretary's review of, the State's mechanized claims processing and information retrieval systems required under section 1396b(r) of this title;
- (H) that to the extent that payment has been made under the State plan for medical assistance in any case where a third party has a legal liability to make payment for such assistance, the State has in effect laws under which, to the extent that payment has been made under the State plan for medical assistance for health care items or services furnished to an individual, the State is considered to have acquired the rights of such individual to payment by any other party for such health care items or services; and

Revised Code of Washington 74.09A.005 Findings, states:

The legislature finds that:

- (1) Simplification in the administration of payment of health benefits is important for the state, providers, and health insurers;
- (2) The state, providers, and health insurers should take advantage of all opportunities to streamline operations through automation and the use of common computer standards;
- (3) It is in the best interests of the state, providers, and health insurers to identify all third parties that are obligated to cover the cost of health care coverage of joint beneficiaries; and
- (4) Health insurers, as a condition of doing business in Washington, must increase their effort to share information with the authority and accept the authority's timely claims consistent with 42 U.S.C. 1396a(a)(25).

Therefore, the legislature declares that to improve the coordination of benefits between the health care authority and health insurers to ensure that medical insurance benefits are properly utilized, a transfer of information between the authority and health insurers should be instituted, and the process for submitting requests for information and claims should be simplified.

Revised Code of Washington 74.09A.020 Computerized information — Provision to health insurers, states:

- 1. The authority shall provide routine and periodic computerized information to health insurers regarding client eligibility and coverage information. Health insurers shall use this information to identify joint beneficiaries. Identification of joint beneficiaries shall be transmitted to the authority. The authority shall use this information to improve accuracy and currency of health insurance coverage and promote improved coordination of benefits.
- 2. To the maximum extent possible, necessary data elements and a compatible database shall be developed by affected health insurers and the authority. The authority shall establish a representative group of health insurers and state agency representatives to develop necessary technical and file specifications to promote a standardized database. The database

shall include elements essential to the authority and its population's health insurance coverage information.

3. If the state and health insurers enter into other agreements regarding the use of common computer standards, the database identified in this section shall be replaced by the new common computer standards.
4. The information provided will be of sufficient detail to promote reliable and accurate benefit coordination and identification of individuals who are also eligible for authority programs.
5. The frequency of updates will be mutually agreed to by each health insurer and the authority based on frequency of change and operational limitations. In no event shall the computerized data be provided less than semiannually.
6. The health insurers and the authority shall safeguard and properly use the information to protect records as provided by law, including but not limited to chapters 42.48, 74.09, 74.04, 70.02, and 42.56 RCW, and 42 U.S.C. Sec. 1396a and 42 C.F.R. Sec. 43 et seq. The purpose of this exchange of information is to improve coordination and administration of benefits and ensure that medical insurance benefits are properly utilized.
7. The authority shall target implementation of this section to those health insurers with the highest probability of joint beneficiaries.

2018-042 **The Health Care Authority did not have adequate internal controls over and did not comply with requirements to ensure certain Medicaid providers were revalidated every five years or that screening and fingerprint-based criminal background check requirements were met.**

Federal Awarding Agency: U.S. Department of Health and Human Services
Pass-Through Entity: None
CFDA Number and Title: 93.775 State Medicaid Fraud Control Units
93.777 State Survey and Certification of Health Care Providers and Suppliers (Title XVIII) Medicare
93.778 Medical Assistance Program (Medicaid; Title XIX)
Federal Award Number: 1805WA5MAP; 1805WA5ADM; 1805WAIMPL; 1805WAINCT
Applicable Compliance Component: Special Tests and Provisions – Provider Eligibility-Provider Revalidation
Questioned Cost Amount: None

Background

Medicaid is a jointly funded state and federal partnership providing coverage for about 1.9 million eligible low-income Washington residents who otherwise might go without medical care. Medicaid is Washington’s largest public assistance program and accounts for about one-third of the State’s federal expenditures. The program spent about \$13.2 billion in federal and state funds during fiscal year 2018.

Provider enrollment

In March 2011, a new federal regulation required state Medicaid agencies to revalidate the enrollment of all Medicaid providers at least every five years. The Centers for Medicare and Medicaid Services (CMS) notified states through an informational bulletin that the revalidation of all providers, enrolled on or before March 25, 2011, must be completed by March 24, 2016.

In January 2016, CMS issued updated guidance to states that extended the deadline for provider revalidation to September 25, 2016. This new deadline applied to all providers enrolled on or before September 25, 2011. After this deadline, all providers must be revalidated every five years from their initial enrollment date. As part of this updated guidance, CMS required states to notify all affected providers of the revalidation requirement by the original March 24, 2016, deadline.

Provider screening risk levels

The first step in revalidating a provider is to determine the provider’s screening risk level. A provider can be designated as one of three risk levels: limited, moderate or high. Each risk level requires progressively greater scrutiny of the provider before it can be revalidated. CMS issued initial guidance

on screening levels for specific provider types. For providers enrolled with both Medicare and Medicaid, state Medicaid agencies must assign providers to the same or higher risk category applicable under Medicare. In addition, certain provider behaviors require a provider to be moved to a higher screening risk level.

The following are the required screening procedures for each of the risk levels:

Limited risk

- Verify that provider meets applicable federal regulations or state requirements for provider type before making an enrollment determination
- Conduct license verifications, including for licenses in states other than where the provider is enrolling
- Conduct database checks to ensure providers continue to meet the enrollment criteria for their provider type

Moderate risk

- Perform the “limited” screening requirements
- Conduct onsite visits

High risk

- Perform the “limited” and “moderate” screening requirements
- Conduct a fingerprint -based criminal background check

According to federal regulation, state Medicaid agencies must adjust the categorical risk level of a particular provider from “limited” or “moderate” to “high” when any of the following situations occur:

- A Medicaid agency imposes a payment suspension on a provider based on credible allegation of fraud, waste or abuse. The provider’s risk remains “high” for 10 years after the date the payment suspension was issued.
- A provider that, upon applying for enrollment or revalidation, is found to have an existing state Medicaid Plan overpayment
- The provider has been excluded by the Office of Inspector General or another state's Medicaid program in the previous 10 years.
- A Medicaid agency or CMS, in the previous six months, lifted a temporary moratorium for the particular provider type and a provider that was prevented from enrolling based on the moratorium applies for enrollment as a provider at any time within six months from the date the moratorium was lifted.

Fingerprint-based criminal background check

In revalidating a provider’s enrollment, the state Medicaid agency must conduct a fingerprint-based criminal background check when the agency has designated a provider as high risk. A high-risk provider or a person with a 5 percent or more direct or indirect ownership interest in the provider is

subject to an FCBC requirement. The deadline to fully-implement a fingerprint-based criminal background check process was June 1, 2016. The full implementation date is the date when the state Medicaid agency is required to have completed each of the following tasks related to fingerprint-based criminal background checks:

- Notify each provider in the high risk category about the fingerprint-based criminal background check requirement
- Collect and use fingerprints to verify whether the provider or any person with a 5 percent or more or indirect ownership interest in the provider has a criminal history in the state or, if it chooses, at the national level
- Take any necessary termination action based on the criminal history data and updated enrollment records to reflect fingerprint-based criminal background check status
- Indicate in the enrollment record for a provider in the high-risk category whether and when the provider passed, failed or failed to respond to the requirement for fingerprint-based criminal background checks

On August 1, 2017, CMS extended the deadline to implement a fingerprint-based criminal background check process to July 1, 2018.

Over 96,000 Medicaid providers were active in Washington during fiscal year 2018. The Health Care Authority (Authority), which administers the state's Medicaid program, paid about \$1.45 billion for fee-for-service claims billed by medical providers. In the prior audit, we reported the Authority did not have adequate internal controls over and did not comply with requirements to ensure Medicaid medical providers were revalidated every five years and screening requirements were met. The prior finding number was 2017-033.

Description of Condition

The Authority did not have adequate internal controls over and did not comply with requirements to ensure Medicaid medical providers were revalidated every five years or that screening and fingerprint-based criminal background check requirements were met.

Provider enrollment

Despite multiple extensions and notifications that CMS issued to states beginning in January 2016, the Authority did not revalidate all medical providers as federal regulations required. The Authority has established a process to revalidate medical providers, but did not have adequate personnel resources to ensure all medical providers were revalidated by the deadline.

Provider screening levels

The Authority did not establish a process to adjust provider screening risk levels.

Fingerprint-based criminal background check

The Authority did not implement a fingerprint-based criminal background check process by the extended deadline of July 1, 2018.

We consider these internal control deficiencies to be a material weakness.

Cause of Condition

The Authority said that limited staff resources were the reason medical providers were not revalidated by their five-year deadline, and that risk adjustment and fingerprint-based criminal background check process were not implemented.

Effect of Condition

The Authority did not revalidate 39,838 out of 55,937 (71 percent) medical providers required to be revalidated as of June 28, 2018.

By not complying with federal provider revalidation, screening and fingerprint-based criminal background check requirements, the Authority is at a higher risk of not detecting when medical providers are ineligible to provide services or be paid with Medicaid funds.

Recommendation

We recommend the Authority:

- Implement internal controls designed to bring it into material compliance with provider revalidation requirements
- Implement a process to adjust providers' screening risk levels
- Implement a process to conduct fingerprint-based criminal background checks for high-risk providers

Authority's Response

The Health Care Authority (HCA) is aware of the current situation with provider revalidation and is closely monitoring with routine reports.

HCA is working on a long-term solution by developing an automated process that will conduct all necessary data matches. The new process is expected to significantly reduce the amount of manual effort required and ensure provider revalidation is performed timely. Until the new automated process is fully implemented, HCA continues to conduct other activities to mitigate the risk of paying ineligible providers.

HCA has prioritized revalidation work, and is making progress towards revalidation compliance, including the re-categorization of high-risk providers. Currently, there are approximately two dozen providers, out of 98,000, that meet the specific criteria to be re-categorized as high risk. Those providers will be subject to the fingerprint based criminal background checks.

Auditor’s Concluding Remarks

We thank the Authority for its cooperation and assistance throughout the audit. We will review the status of the Authority’s corrective action during our next audit.

Applicable Laws and Regulations

Title 2 U.S. Code of Federal Regulations Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance) establishes the following applicable requirements:

Section 200.303 Internal controls.

The non-Federal entity must:

- (a) Establish and maintain effective internal control over the Federal award that provides reasonable assurance that the non-Federal entity is managing the Federal award in compliance with Federal statutes, regulations, and the terms and conditions of the Federal award. These internal controls should be in compliance with guidance in “Standards for Internal Control in the Federal Government” issued by the Comptroller General of the United States or the “Internal Control Integrated Framework”, issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).
- (b) Comply with Federal statutes, regulations, and the terms and conditions of the Federal awards.
- (d) Take prompt action when instances of noncompliance are identified including noncompliance identified in audit findings.

Section 200.516 Audit findings, states in part:

- (a) *Audit findings reported.* The auditor must report the following as audit findings in a schedule of findings and questioned costs:
 - (1) Significant deficiencies and material weaknesses in internal control over major programs and significant instances of abuse relating to major programs. The auditor’s determination of whether a deficiency in internal control is a significant deficiency or material weakness for the purpose of reporting an audit finding is in relation to a type of compliance requirement for a major program identified in the Compliance Supplement.
 - (2) Material noncompliance with the provisions of Federal statutes, regulations, or the terms and conditions of Federal awards related to a major program. The auditor’s determination of whether a noncompliance with the provisions of Federal statutes, regulations, or the terms and conditions of Federal awards is material for the purpose of reporting an audit finding is in relation to a type of compliance requirement for a major program identified in the compliance supplement.

The American Institute of Certified Public Accountants defines significant deficiencies and material weaknesses in internal controls over compliance in its *Codification of Statements on Auditing Standards*, section 935, Compliance Audits, as follows:

.11 For purposes of adapting GAAS to a compliance audit, the following terms have the meanings attributed as follows: ...

Deficiency in internal control over compliance. A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance on a timely basis. A deficiency in design exists when (a) a control necessary to meet the control objective is missing, or (b) an existing control is not properly designed so that, even if the control operates as designed, the control objective would not be met. A deficiency in operation exists when a properly designed control does not operate as designed or the person performing the control does not possess the necessary authority or competence to perform the control effectively.

Material weakness in internal control over compliance. A deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a compliance requirement will not be prevented, or detected and corrected, on a timely basis. In this section, a reasonable possibility exists when the likelihood of an event occurring is either reasonably possible or probable as defined as follows:

Reasonably possible. The chance of the future event or events occurring is more than remote but less than likely.

Probable. The future event or events are likely to occur.

Significant deficiency in internal control over compliance. A deficiency, or a combination of deficiencies, in internal control over compliance that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

Material noncompliance. In the absence of a definition of material noncompliance in the governmental audit requirement, a failure to follow compliance requirements or a violation of prohibitions included in the applicable compliance requirements that results in noncompliance that is quantitatively or qualitatively material, either individually or when aggregated with other noncompliance, to the affected government program.

Title 42 U.S. Code of Federal Regulations section 455 Subpart E – Provider Screening and Enrollment, states in part:

Section 455.414 Revalidation of enrollment

The State Medicaid agency must revalidate the enrollment of all providers regardless of provider type at least every 5 years.

Section 455.434 Criminal background checks

The State Medicaid agency -

- (a) As a condition of enrollment, must require providers to consent to criminal background checks including fingerprinting when required to do so under State law

or by the level of screening based on risk of fraud, waste or abuse as determined for that category of provider.

- (b) Must establish categorical risk levels for providers and provider categories who pose an increased financial risk of fraud, waste or abuse to the Medicaid program.
 - (1) Upon the State Medicaid agency determining that a provider, or a person with a 5 percent or more direct or indirect ownership interest in the provider, meets the State Medicaid agency's criteria hereunder for criminal background checks as a “high” risk to the Medicaid program, the State Medicaid agency will require that each such provider or person submit fingerprints.
 - (2) The State Medicaid agency must require a provider, or any person with a 5 percent or more direct or indirect ownership interest in the provider, to submit a set of fingerprints, in a form and manner to be determined by the State Medicaid agency, within 30 days upon request from CMS or the State Medicaid agency.

Section 455.450 Screening levels for Medicaid providers.

A State Medicaid agency must screen all initial applications, including applications for a new practice location, and any applications received in response to a re-enrollment or revalidation of enrollment request based on a categorical risk level of “limited,” “moderate,” or “high.” If a provider could fit within more than one risk level described in this section, the highest level of screening is applicable.

- (a) Screening for providers designated as limited categorical risk. When the State Medicaid agency designates a provider as a limited categorical risk, the State Medicaid agency must do all of the following:
 - (1) Verify that a provider meets any applicable Federal regulations, or State requirements for the provider type prior to making an enrollment determination.
 - (2) Conduct license verifications, including State licensure verifications in States other than where the provider is enrolling, in accordance with § 455.412.
 - (3) Conduct database checks on a pre- and post-enrollment basis to ensure that providers continue to meet the enrollment criteria for their provider type, in accordance with § 455.436.
- (b) Screening for providers designated as moderate categorical risk. When the State Medicaid agency designates a provider as a “moderate” categorical risk, a State Medicaid agency must do both of the following:
 - (1) Perform the “limited” screening requirements described in paragraph (a) of this section.
 - (2) Conduct on-site visits in accordance with § 455.432.
- (c) Screening for providers designated as high categorical risk. When the State Medicaid agency designates a provider as a “high” categorical risk, a State Medicaid agency must do both of the following:
 - (1) Perform the “limited” and “moderate” screening requirements described in paragraphs (a) and (b) of this section.
 - (2) (i) Conduct a criminal background check; and (ii) Require the submission of a set of fingerprints in accordance with § 455.434.
- (d) Denial or termination of enrollment. A provider, or any person with 5 percent or greater direct or indirect ownership in the provider, who is required by the State

Medicaid agency or CMS to submit a set of fingerprints and fails to do so may have its -

- (1) Application denied under § 455.434; or
 - (2) Enrollment terminated under § 455.416.
- (e) Adjustment of risk level. The State agency must adjust the categorical risk level from “limited” or “moderate” to “high” when any of the following occurs:
- (1) The State Medicaid agency imposes a payment suspension on a provider based on credible allegation of fraud, waste or abuse, the provider has an existing Medicaid overpayment, or the provider has been excluded by the OIG or another State's Medicaid program within the previous 10 years.
 - (2) The State Medicaid agency or CMS in the previous 6 months lifted a temporary moratorium for the particular provider type and a provider that was prevented from enrolling based on the moratorium applies for enrollment as a provider at any time within 6 months from the date the moratorium was lifted.

Centers for Medicare and Medicaid Services, Center for Medicaid and CHIP Services, CMCS Informational Bulletin, dated December 21, 2011, states in part:

The Federal regulation at 42 CFR 455.414 requires States, beginning March 25, 2011, to complete revalidation of enrollment for all providers, regardless of provider type, at least every five years. Based upon this requirement, States must complete the revalidation process of all provider types by March 24, 2016.

Centers for Medicare and Medicaid Services (CMS) Sub Regulatory Guidance for State Medicaid Agencies (SMA): Revalidation (2016-001) states in part:

The federal regulation at 42 CFR 455.414 requires that state Medicaid agencies revalidate the enrollment of all providers, regardless of provider types, at least every 5 years. The regulation was effective March 25, 2011. Based on this requirement, in a December 23, 2011 CMCS Informational Bulletin, we directed states to complete the revalidation process of all provider types by March 24, 2016.

The purpose of this guidance is to revise previous guidance in order to align Medicare and Medicaid revalidation activities to the greatest extent possible. We are revising that previous guidance to now require a two-step deadline under which states must notify all affected providers of the revalidation requirement by the original March 24, 2016 deadline, and must have completed the revalidation process by a new deadline of September 25, 2016.

...

- (3) Deadline for SMA to revalidate providers enrolled on or before September 25, 2011. The Federal regulation at 42 CFR § 455.414 requires states, beginning March 25, 2011, to revalidate the enrollment of all Medicaid providers, regardless of provider type, at least every five years. Based upon this requirement, by March 24, 2016, states must notify providers that were enrolled on or before March 25, 2011 that they must revalidate their enrollment. On March 25, 2016, states that have notified all providers subject to the revalidation requirement will be considered compliant with the revalidation activities required as of that date.

2018-043

The Health Care Authority did not have adequate internal controls over and did not comply with requirements to ensure Medicaid Service Verifications were performed for eligible nursing home claims.

Federal Awarding Agency: U.S. Department of Health and Human Services
Pass-Through Entity: None
CFDA Number and Title: 93.775 State Medicaid Fraud Control Units
93.777 State Survey and Certification of Health Care Providers and Suppliers (Title XVIII) Medicare
93.778 Medical Assistance Program (Medicaid; Title XIX)
Federal Award Number: 1805WA5MAP; 1805WA5ADM; 1805WAIMPL; 1805WAINCT
Applicable Compliance Component: Special Tests and Provisions – Utilization Control and Program Integrity
Known Questioned Cost Amount: None

Background

Medicaid is a jointly funded state and federal partnership providing coverage for about 1.9 million eligible low-income Washington residents who otherwise might go without medical care. Medicaid is Washington’s largest public assistance program and accounts for about one-third of the state’s federal expenditures. The program spent about \$12.7 billion in federal and state funds during fiscal year 2018.

For states, such as Washington, that use an automated claims processing system (ProviderOne), federal regulations require a specific method be in place to verify with Medicaid clients that they received services billed by providers. The intent is to improve program integrity and identify potential fraud and abuse in the Medicaid program.

The specific verification method involves sending individual written notices, within 45 days of payment, to all or a sample group of Medicaid clients whose claims were processed through ProviderOne. Medical, nursing home and social service claims are subject to the Medicaid service verification process. The only allowable exclusion is claims for confidential services. In fiscal year 2018, the state Medicaid program spent over \$4.5 billion for medical, nursing home and social service claims.

The Health Care Authority (Authority) processes medical claims, and the Department of Social and Health Services (Department) processes social service and nursing home claims. As the owner of the state’s automated claims processing system, the Authority is ultimately responsible to ensure all eligible claims are included in the Medicaid service verification survey process.

In state fiscal year 2018, the Authority mailed Medicaid medical and social service verification surveys to randomly selected clients every month. Clients who received the survey were selected based on payments made through ProviderOne.

If the Authority identifies a credible suspicion of fraud or abuse, it must forward the information to the Attorney General's Office, Medicaid Fraud Control Unit, for investigation.

In a prior audit, we reported the Authority did not ensure eligible nursing home claims were included in the Medicaid service verification process. The prior finding number was 2017-034.

Description of Condition

We found the Authority did not have adequate internal controls over and did not comply with requirements to ensure Medicaid Service Verifications were performed for eligible nursing home claims.

Although the Authority established an adequate process to select medical claims processed through ProviderOne, it did not include nursing home claims in any random monthly sample between July 2017 and February 2018 – eight of the 12 months during the audit period. Nursing home claims account for about 8 percent of total fee-for-service claims paid through ProviderOne.

We consider this internal control deficiency to be a material weakness.

Cause of Condition

The Authority excluded nursing home claims because these facilities are paid a fixed monthly rate and it felt the return on investment was low. It believed identifying potential fraud for this population could be accomplished through other means and that by excluding this population, it could select higher-risk providers to include in this process.

Effect of Condition

We used a non-statistical sampling method and randomly selected five monthly reports out of a total population of 12 monthly reports. We found three out of five tested monthly reports, or 60 percent, did not include the nursing home claims.

By not designing its service verification process to include all required claims, the Authority is at an increased risk of not detecting potential Medicaid fraud.

Recommendation

We recommend the Authority design its service verification survey process to include all required ProviderOne claims.

Authority's Response

The Authority does not agree that the exclusion of nursing homes in the survey population is an indication of control deficiency. The Authority strategically excluded nursing homes in order to conduct targeted, risk-based verifications with high return rates. From a compliance standpoint, the Authority believes federal regulations allow flexibility for grantees to adopt a more effective approach.

The Authority will continue to consult with the federal grantor to obtain clarification. As of March 2018, nursing homes are included in the universe of ProviderOne claims until definitive federal guidance is obtained.

Auditor's Concluding Remarks

We thank the Authority for its cooperation and assistance throughout the audit. We will review the status of the Authority's corrective action during our next audit.

Applicable Laws and Regulations

Title 2 U.S. Code of Federal Regulations Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance) establishes the following applicable requirements:

Section 200.303 Internal controls, states in part:

The non-Federal entity must:

- (a) Establish and maintain effective internal control over the Federal award that provides reasonable assurance that the non-Federal entity is managing the Federal award in compliance with Federal statutes, regulations, and the terms and conditions of the Federal award. These internal controls should be in compliance with guidance in "Standards for Internal Control in the Federal Government" issued by the Comptroller General of the United States or the "Internal Control Integrated Framework", issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).
- (b) Comply with Federal statutes, regulations, and the terms and conditions of the Federal awards.
- (d) Take prompt action when instances of noncompliance are identified including noncompliance identified in audit findings.

Section 200.516 Audit findings, states in part:

- (a) *Audit findings reported.* The auditor must report the following as audit findings in a schedule of findings and questioned costs:
 - (1) Significant deficiencies and material weaknesses in internal control over major programs and significant instances of abuse relating to major programs. The auditor's determination of whether a deficiency in internal control is a significant deficiency or material weakness for the purpose of reporting an audit finding is in relation to a type of compliance requirement for a major program identified in the Compliance Supplement.

- (2) Material noncompliance with the provisions of Federal statutes, regulations, or the terms and conditions of Federal awards related to a major program. The auditor's determination of whether a noncompliance with the provisions of Federal statutes, regulations, or the terms and conditions of Federal awards is material for the purpose of reporting an audit finding is in relation to a type of compliance requirement for a major program identified in the compliance supplement.

The American Institute of Certified Public Accountants defines significant deficiencies and material weaknesses in internal controls over compliance in its *Codification of Statements on Auditing Standards*, section 935, Compliance Audits, as follows:

.11 For purposes of adapting GAAS to a compliance audit, the following terms have the meanings attributed as follows: ...

Deficiency in internal control over compliance. A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance on a timely basis. A deficiency in design exists when (a) a control necessary to meet the control objective is missing, or (b) an existing control is not properly designed so that, even if the control operates as designed, the control objective would not be met. A deficiency in operation exists when a properly designed control does not operate as designed or the person performing the control does not possess the necessary authority or competence to perform the control effectively.

Material weakness in internal control over compliance. A deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a compliance requirement will not be prevented, or detected and corrected, on a timely basis. In this section, a reasonable possibility exists when the likelihood of an event occurring is either reasonably possible or probable as defined as follows:

Reasonably possible. The chance of the future event or events occurring is more than remote but less than likely.

Probable. The future event or events are likely to occur.

Significant deficiency in internal control over compliance. A deficiency, or a combination of deficiencies, in internal control over compliance that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

Material noncompliance. In the absence of a definition of material noncompliance in the governmental audit requirement, a failure to follow compliance requirements or a violation of prohibitions included in the applicable compliance requirements that results in noncompliance that is quantitatively or qualitatively material, either individually or when aggregated with other noncompliance, to the affected government program.

Title 42, U.S. Code of Federal Regulations, Chapter IV, Subpart C—Mechanized Claims Processing and Information Retrieval Systems, section 433.110 Basis, purpose and applicability, states in part:

- (a) This subpart implements the following sections of the Act:

- (1) Section 1903(a)(3) of the Act, which provides for FFP in State expenditures for the design, development, or installation of mechanized claims processing and information retrieval systems and for the operation of certain systems. Additional HHS regulations and CMS procedures for implementing these regulations are in 45 CFR part 75, 45 CFR part 95, subpart F, and part 11, State Medicaid Manual; and
- (2) Section 1903(r) of the Act, which imposes certain standards and conditions on mechanized claims processing and information retrieval systems (including eligibility determination systems) in order for these systems to be eligible for Federal funding under section 1903(a) of the Act.

Title 42, U.S. Code of Federal Regulations, Section 433.116 FFP for operation of mechanized claims processing and information retrieval systems, states in part:

- (a) Subject to paragraph (j) of this section, FFP is available at 75 percent of expenditures for operation of a mechanized claims processing and information retrieval system approved by CMS, from the first day of the calendar quarter after the date the system met the conditions of initial approval, as established by CMS (including a retroactive adjustment of FFP if necessary to provide the 75 percent rate beginning on the first day of that calendar quarter). Subject to 45 CFR 95.611(a), the State shall obtain prior written approval from CMS when it plans to acquire ADP equipment or services, when it anticipates the total acquisition costs will exceed thresholds, and meets other conditions of the subpart.
- (b) CMS will approve enhanced FFP for system operations if the conditions specified in paragraphs (c) through (i) of this section are met.
- (c) The conditions of §433.112(b)(1) through (22) must be met at the time of approval.
- (d) The system must have been operating continuously during the period for which FFP is claimed.
- (e) The system must provide individual notices, within 45 days of the payment of claims, to all or a sample group of the persons who received services under the plan.
- (f) The notice required by paragraph (e) of this section—
 - (1) Must specify—
 - (i) The service furnished;
 - (ii) The name of the provider furnishing the service;
 - (iii) The date on which the service was furnished; and
 - (iv) The amount of the payment made under the plan for the service; and
 - (2) Must not specify confidential services (as defined by the State) and must not be sent if the only service furnished was confidential.
- (g) The system must provide both patient and provider profiles for program management and utilization review purposes.
- (h) If the State has a Medicaid fraud control unit certified under section 1903(q) of the Act and §455.300 of this chapter, the Medicaid agency must have procedures to assure that information on probable fraud or abuse that is obtained from, or developed by, the system is made available to that unit. (See §455.21 of this chapter for State plan requirements.)

Title 42, U.S. Code of Federal Regulations, Section 455.1 Basis and scope, states in part:

This part sets forth requirements for a State fraud detection and investigation program, and for disclosure of information on ownership and control.

- (a) Under the authority of sections 1902(a)(4), 1903(i)(2), and 1909 of the Social Security Act, Subpart A provides State plan requirements for the identification, investigation, and referral of suspected fraud and abuse cases. In addition, the subpart requires that the State—
 - (1) Report fraud and abuse information to the Department; and
 - (2) Have a method to verify whether services reimbursed by Medicaid were actually furnished to beneficiaries.

Title 42, U.S. Code of Federal Regulations, Section 455.14 Preliminary investigation states:

If the agency receives a complaint of Medicaid fraud or abuse from any source or identifies any questionable practices, it must conduct a preliminary investigation to determine whether there is sufficient basis to warrant a full investigation.

Title 42, U.S. Code of Federal Regulations, Section 455.20 Beneficiary verification procedure states:

- (a) The agency must have a method for verifying with beneficiaries whether services billed by providers were received.
- (b) In States receiving Federal matching funds for a mechanized claims processing and information retrieval system under part 433, subpart C, of this subchapter, the agency must provide prompt written notice as required by §433.116 (e) and (f).

Health Care Authority, Office of Program Integrity (OPI) Procedure No. 2.1.2 states:

Medical Service Verification (MSV) Procedure
Procedure:

- I. Selection and Issuance of MSVs.
 - A. Each month, using an automated random selection process, ProviderOne will issue 400 MSV forms to Washington Apple Health fee-for-service medical, nursing home and social service clients.
 - B. MSV mailings will:
 - 1. Exclude clients receiving confidential services
 - 2. Include a self-addressed stamped envelope for client to return to HCA;
 - 3. Include a Language Assistance Sheet; and
 - 4. Identify the specific service recipient
 - C. ProviderOne will create a report of all MSVs mailed.
 - 1. Report will be sent to PI Intake Coordinator and DSHS
 - 2. PI Intake Coordinator will upload the report into the PI Intake Database
- II. Receipt of MSVs
 - A. Each returned MSV will be scanned into the ProviderOne system, batched by the date received and submitted to the Intake Coordinator

- B. All social service MSVs will be forwarded to DSHS, per Service Level Agreement (SLA), for processing.
 - C. The Intake Coordinator will log all returned medical and nursing home MSVs into the PI Intake Database, whether services are designated as received or not.
 - D. The Intake Coordinator will refer all leads from medical and nursing home MSVs with potential fraud, waste or abuse to the appropriate Utilization Analyst for further research and analysis.
- III. The Utilization Analyst will:
- A. Review the work of the Intake Coordinator, conduct further research and determine if a preliminary investigation is warranted.
 - B. Refer lead back to Intake Coordinator to close the MSV without action if a preliminary investigation is not required; or
 - C. Open a case in the Optum Case Tracking Module for assignment and conduct the preliminary investigation.
 - D. Follow the procedure for preliminary investigation and refer to CMT or for full investigation if indicated.
- IV. Quality Control and Reporting

2018-044 The Health Care Authority did not have adequate internal controls to ensure its federal draws for the Medicaid Transformation Demonstration project were adequately supported.

Federal Awarding Agency: U.S. Department of Health and Human Services
Pass-Through Entity: None
CFDA Number and Title: 93.775 State Medicaid Fraud Control Units
93.777 State Survey and Certification of Health Care Providers and Suppliers (Title XVIII) Medicare
93.778 Medical Assistance Program (Medicaid; Title XIX)
Federal Award Number: 1805WA5MAP; 1805WA5ADM; 1805WAIMPL; 1805WAINCT
Applicable Compliance Component: Activities Allowed / Allowable Costs Cost Principles
Known Questioned Cost Amount: None

Background

Medicaid is a jointly funded state and federal partnership providing coverage for about 1.9 million eligible low-income Washington residents who otherwise might go without medical care. Medicaid is Washington’s largest public assistance program and accounts for about one-third of the State’s federal expenditures. The program spent about \$12.7 billion in federal and state funds during fiscal year 2018. Washington’s Medicaid program is overseen by the Health Care Authority (Authority).

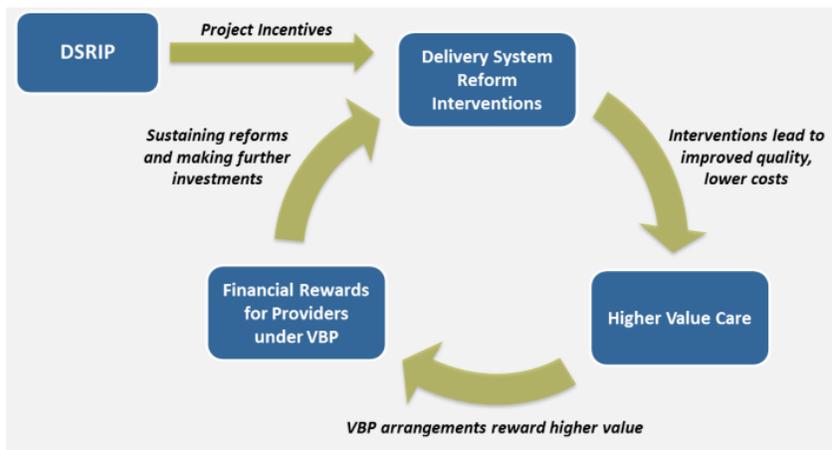
Medicaid Transformation Demonstration Project

In 2017, the Authority and the Centers for Medicare and Medicaid Services (CMS) finalized an agreement for a five-year Medicaid Transformation Demonstration (MTD) project to improve the state’s health care systems, provide better health care and control costs. From January 2017 to December 2021, the state is eligible to receive up to \$1.5 billion in federal investment to restructure, improve and enhance the Apple Health (Medicaid) service delivery system.

The MTD is the result of a Section 1115 waiver, which is a contract between the federal and state governments that waives certain Medicaid requirements, as long as the state can demonstrate budget neutrality by ensuring each dollar spent for Initiative one of the MTD is offset by equal or greater savings in Medicaid expenditures. The state can use these funds for innovative projects, activities and services that would not otherwise be allowed. It is not a grant; the state must show that it will not spend more federal dollars on its Medicaid program than it would have spent without the waiver. The waiver contains a list of special terms and conditions (STCs) the state must comply with.

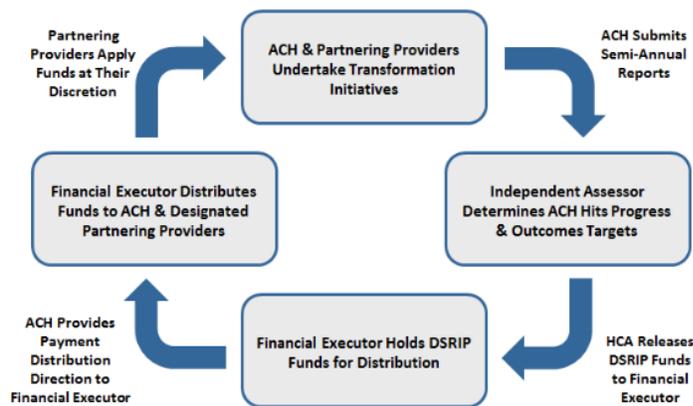
The first initiative of the MTD is to transform the health system at the local level. Each region in the state is led by an Accountable Community of Health (ACH). Because the MTD federal investment is

not a grant, ACHs and their partners receive funds only after they achieve certain milestones in approved project plans submitted to the Authority. The Delivery System Reform Incentive Payment (DSRIP) program is one of the foundations of the MTD. Washington is using DSRIP to invest in projects that will help medical providers successfully adopt value-based payment (VBP) contracts with Medicaid managed care organizations. VBP contracts award providers for delivering high-quality, integrated and whole-person care, instead of just the amount of care they provide.



Once funds are earned by a region, ACHs determine which of its partners will receive funds, when the funds are distributed by the Authority, and in what amounts. Decisions are made through consultation with regional partners and public meetings.

As seen in the chart below, the Authority releases each region’s earned funds to a third-party financial executor based on the independent assessor’s determination of regional achievement of the reporting and/or performance targets. The financial executor then distributes regional funds based on the ACH’s direction.



In fiscal year 2018, the Authority spent about \$199 million in federal funds and about \$33 in local funds for the MTD.

Support for federal funding

There are two ways that CMS has authorized the Authority to provide the required match in order to draw down federal funds: Certified Public Expenditures from Designated State Health Programs (DSHP) and intergovernmental transfers (IGT).

DSHPs are existing publicly-funded health programs that support low income/uninsured individuals. DSHP programs must be funded completely with state or local government dollars without in-kind contributions.

IGTs are an approved methodology to provide required match for federal claiming. They are transfers of public funds between governmental entities, such as from a county or public hospital, to the Authority. The source of funding for IGTs is approved in advance by CMS.

Certified public expenditures

Within the MTD STCs is a protocol the Authority must follow when drawing down federal funds based on DSHP expenses. The state uses certified public expenditures (CPE) as the funding mechanism to claim federal match for approved DSHPs. The responsible entities, such as state agencies, counties and cities that manage the DSHPs, must submit expenditure information on a monthly and annual basis to the Authority. The responsible entities must also certify and attest that the reported expenditures are allowable to be claimed as CPE. Along with the total monthly expenses, the entities must provide the Authority with supporting documentation showing how the funds were spent.

The STCs contain a list of expenses that are not allowed to be claimed as CPE. Some examples include construction costs, services to undocumented individuals, administrative costs and funds from other federal grants. The Authority must obtain the signed CPE reports and supporting documentation before using it as support for drawing down federal funds. Also, the reports must not contain accrued expenses, only actual DSHP payments (cash-basis).

According to the STCs, the Authority must contract with an independent auditor to annually validate the accuracy of its federal claims. The Authority must also have program integrity efforts in place to ensure there is no duplication of federal funding for any aspect of the MTD.

Description of Condition

The Health Care Authority did not have adequate internal controls to ensure its federal draws for the MTD were adequately supported.

We confirmed the Authority obtained signed attestations report forms from the responsible entities that managed the DSHPs. However, the Authority did not implement procedures to verify the reported expenditures were allowable to claim as CPE.

Additionally, the Authority did not contract with an external auditor to validate the accuracy of federal claims or establish program integrity efforts to ensure there is no duplication of federal funding for any aspect of the MTD as required in the STCs.

We consider this internal control deficiency to be a material weakness. This condition was not reported in the prior audit.

Cause of Condition

The Authority experienced significant turnover in MTD program staff during the audit period. The Authority has not developed its own policies and procedures that describes program staff roles and responsibilities. The Authority said that the staff turnover was a contributing factor in why an external auditor was not contracted with as required in the STCs. Funds have been budgeted to proceed with the contracting process and the Authority said it has started the solicitation process.

The Authority did not establish CPE reporting guidelines for responsible entities of DSHPs. This led to the supporting documentation to vary for each DSHP. In some cases, the supporting documentation was not specific enough to determine if the reported expenses included unallowable activities.

Effect of Condition

In total, the Authority collected \$197,352,390 in CPE that covered calendar year one of the five year demonstration period. We examined the supporting documentation submitted by the responsible entities of the DSHPs and found some contained expenses that were not allowed to be claimed as CPE.

Specifically we found:

- \$1,091,619 in CPE was reported by four entities for administrative expenses
- \$53,927 in CPE was reported by one entity for accrued expenses
- \$2,254,237 in CPE for a DSHP was recorded, but the responsible entity did not provide supporting documentation with its monthly reports as required by the STCs

The Authority provided evidence that it had collected sufficient CPE, not including the unallowable expenditures identified by the audit, to support its federal draw downs for calendar year 1 of the demonstration. Therefore, we will not question these costs.

Although we are not questioning the costs, we are including this information in the finding to provide context to show that the Authority's system of internal controls did not identify the unallowable expenses.

Recommendations

We recommend the Authority:

- Contract with an external auditor to validate the accuracy of its federal claims
- Establish program integrity processes to ensure there is no duplication of federal funding for the MTD
- Establish internal policies and procedures for the MTD that, at minimum, describe the roles and responsibilities of staff
- Establish reporting guidelines for responsible entities of DSHPs to ensure they report consistent and detailed supporting documentation for their CPE

Authority's Response

While the Authority agrees with the State Auditor's Office (SAO) in not questioning the costs under the Effect of Condition, the Authority disagrees with the SAO in reporting the finding of \$2,254,237 in Certified Public Expenditures (CPE) as unallowable for Designated State Health Program (DSHP) claiming. The responsible entity did provide supporting documentation with its report. In addition, the Authority provided SAO with evidence that federal funds were not drawn down using that entity's CPE. The Authority agrees with the SAO on the Cause of the Condition. The Authority will be working on filling staff vacancies and clearly defining policies and procedures for staff roles. We are in the process

of starting the procurement for the Independent External Auditor. The Authority is also working on defining administrative costs for DSHP.

The Authority will consult with the U.S. Department of Health and Human Services regarding establishing a process for program integrity.

Auditor’s Concluding Remarks

We included information about the unallowable CPE identified during the audit because the Authority’s internal controls were not adequate to identify them. We will follow up during our next audit to determine if the Authority has taken corrective action on the matters reported in the finding.

Applicable Laws and Regulations

Title 2 U.S. Code of Federal Regulations Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance) establishes the following applicable requirements:

Section 200.303 Internal controls, states in part:

The non-Federal entity must:

- (a) Establish and maintain effective internal control over the Federal award that provides reasonable assurance that the non-Federal entity is managing the Federal award in compliance with Federal statutes, regulations, and the terms and conditions of the Federal award. These internal controls should be in compliance with guidance in “Standards for Internal Control in the Federal Government” issued by the Comptroller General of the United States or the “Internal Control Integrated Framework”, issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).

Section 200.516 Audit findings, states in part:

- (a) *Audit findings reported.* The auditor must report the following as audit findings in a schedule of findings and questioned costs:
 - (1) Significant deficiencies and material weaknesses in internal control over major programs and significant instances of abuse relating to major programs. The auditor’s determination of whether a deficiency in internal control is a significant deficiency or material weakness for the purpose of reporting an audit finding is in relation to a type of compliance requirement for a major program identified in the Compliance Supplement.

The American Institute of Certified Public Accountants defines significant deficiencies and material weaknesses in internal controls over compliance in its *Codification of Statements on Auditing Standards*, section 935, Compliance Audits, as follows:

- .11 For purposes of adapting GAAS to a compliance audit, the following terms have the meanings attributed as follows: ...

Deficiency in internal control over compliance. A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow

management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance on a timely basis. A deficiency in design exists when (a) a control necessary to meet the control objective is missing, or (b) an existing control is not properly designed so that, even if the control operates as designed, the control objective would not be met. A deficiency in operation exists when a properly designed control does not operate as designed or the person performing the control does not possess the necessary authority or competence to perform the control effectively.

Material weakness in internal control over compliance. A deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a compliance requirement will not be prevented, or detected and corrected, on a timely basis. In this section, a reasonable possibility exists when the likelihood of an event occurring is either reasonably possible or probable as defined as follows:

Reasonably possible. The chance of the future event or events occurring is more than remote but less than likely.

Probable. The future event or events are likely to occur.

Significant deficiency in internal control over compliance. A deficiency, or a combination of deficiencies, in internal control over compliance that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

Office of Management and Budget OMB Uniform Guidance, Compliance Supplement for 2017, *Part 4 – Agency Program Requirements, 4.93.778 Medicaid Cluster*, states in part:

General Audit Approach for Medicaid Payments

To be allowable, Medicaid costs for medical services must be (1) covered by the State plan and waivers; (2) reviewed by the State consistent with the State's documented procedures and system for determining medical necessity of claims; (3) properly coded; and (4) paid at the rate allowed by the State plan. Additionally, Medicaid costs must be net of beneficiary cost-sharing obligations and applicable credits (e.g., insurance, recoveries from other third parties who are responsible for covering the Medicaid costs, and drug rebates), paid to eligible providers, and only provided on behalf of eligible individuals.

2018-045 The Health Care Authority claimed federal funds for Medicaid expenditures that exceeded the two-year time limit.

Federal Awarding Agency: U.S. Department of Health and Human Services
Pass-Through Entity: None
CFDA Number and Title: 93.775 State Medicaid Fraud Control Units
93.777 State Survey and Certification of Health Care Providers and Suppliers (Title XVIII) Medicare
93.778 Medical Assistance Program (Medicaid; Title XIX)
Federal Award Number: 1805WA5MAP; 1805WA5ADM; 1805WAIMPL; 1805WAINCT
Applicable Compliance Component: Period of Performance
Known Questioned Cost Amount: \$ 2,095,931

Background

Medicaid is a jointly funded state and federal partnership providing coverage for about 1.9 million eligible low-income Washington residents who otherwise might go without medical care. Medicaid is Washington’s largest public assistance program and accounts for about one-third of the State’s federal expenditures. The program spent about \$12.7 billion in federal and state funds during fiscal year 2018.

Federal law establishes a two-year limit for a state to claim federal funds for Medicaid expenditures. For Medicaid funds to be reimbursed, claims must be filed to the federal grantor within two years after the calendar quarter in which the state agency made the expenditures. Exceptions to the two-year limit are:

- Any claim for an adjustment to prior-year costs
- Any claim resulting from an audit exception
- Any claim resulting from a court-ordered retroactive payment
- Any claim for which the Secretary decides there was good cause for the state's not filing it within the time limit

The Health Care Authority (Authority), Washington’s Medicaid agency, draws federal funds for Medicaid expenditures made by the Authority and the Department of Social and Health Services on a weekly basis. The Authority’s fiscal unit prepares a CMS-64 Quarterly Statement of Expenditures for the Medical Assistance Program report. While preparing the report, the unit analyzes Medicaid expenditures to ensure the report includes only expenditures that are within the two-year limit. If the unit finds any Medicaid claimed expenditures that exceed the two-year limit, it processes a journal voucher to pay back the claimed federal portion of the expenditures to the federal grantor.

In fiscal year 2018, the Authority claimed about \$8.1 billion in federal dollars for the Medicaid program.

Description of Condition

We found the Authority had adequate internal controls to ensure it claimed federal funds for expenditures that were within the two-year time limit. However, we reviewed all four quarterly CMS-64 reports and supporting documentation submitted for fiscal year 2018 and found that the Authority claimed \$2,095,931 in Medicaid expenditures that were past the two-year time limit.

The following table summarizes our results:

CMS-64 Reporting Quarter for State Fiscal Year 2018	Health Care Authority	Department of Social and Health Services	Total
Quarter 1	\$52,779	\$ 746,921	\$799,701
Quarter 2	\$2,679	\$5,633	\$8,311
Quarter 3	\$10,331	\$149	\$10,480
Quarter 4	\$1,277,271	\$168	\$1,277,439
Total	\$1,343,060	\$752,871	\$2,095,931

The Authority’s fiscal unit identified the federal claims made for Medicaid expenditures that were past the two-year time limit when the CMS-64 reports were prepared. The expenditures were excluded from the quarterly reports due to the two-year limit. However, the unit did not process journal vouchers to pay back the unallowed federal claimed amounts to its federal grantor.

This condition was not reported in the prior audit.

Cause of Condition

The Authority said paying back the federal funds that are identified as outside the two-year limit is not always done at the end of each quarter. While that process is always preferable, the Authority’s workload and limited resources did not allow it to complete this promptly.

Effect of Condition and Questioned Costs

The federal grantor does not allow a state to claim federal funds for Medicaid expenditures that are past the two-year limit. We are questioning the \$2,095,931 in federal funds claimed by the Authority that exceeded the two-year limit.

We question costs when we find an agency has not complied with grant regulations or when it does not have adequate documentation to support its expenditures.

Recommendation

We recommend the Authority consult with the U.S. Department of Health and Human Services to discuss whether the questioned costs identified in the audit should be repaid.

Authority's Response

The authority agrees with the finding that journal vouchers to reduce federal expenditures for amounts outside the two-year claiming period were not processed during the audit period.

The identification of these amounts is done quarterly, based solely on federal fiscal year, and are not reported on the claim. Prior to the transfer of these charges to state funds, considerable research is required to determine if the charge is in fact unallowable. Due to limited staffing, and the amount of research required, the actual transfer does not always occur timely. These adjustments, if appropriate, are done during the award close-out process and the federal funds are returned.

Auditor's Concluding Remarks

We thank the Authority for its cooperation and assistance throughout the audit. We will review the status of the Authority's corrective action during our next audit.

Applicable Laws and Regulations

Title 2 U.S. Code of Federal Regulations Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance) establishes the following applicable requirements:

Section 200.53 Improper Payments states:

- (a) *Improper payment* means any payment that should not have been made or that was made in an incorrect amount (including overpayments and underpayments) under statutory, contractual, administrative, or other legally applicable requirements; and
- (b) *Improper payment* includes any payment to an ineligible party, any payment for an ineligible good or service, any duplicate payment, any payment for a good or service not received (except for such payments where authorized by law), any payment that does not account for credit for applicable discounts, and any payment where insufficient or lack of documentation prevents a reviewer from discerning whether a payment was proper.

Section 200.403 Factors affecting Allowability of costs.

Except where otherwise authorized by statute, costs must meet the following general criteria in order to be allowable under Federal awards.

- (a) Be necessary and reasonable for the performance of the Federal award and be allocable thereto under these principles.
- (b) Conform to any limitations or exclusions set forth in these principles or in the Federal award as to types or amount of cost items.

- (c) Be consistent with policies and procedures that apply uniformly to both federally-financed and other activities of the non-Federal entity.
- (d) Be accorded consistent treatment. A cost may not be assigned to a Federal award as a direct cost if any other cost incurred for the same purpose in like circumstances has been allocated to the Federal award as an indirect cost.
- (e) Be determined in accordance with generally accepted accounting principles (GAAP), except, for state and local governments and Indian tribes only, as otherwise provided for in this part.
- (f) Not be included as a cost or used to meet cost sharing or matching requirements of any other federally-financed program in either the current or a prior period. See also §200.306 Cost sharing or matching paragraph (b).
- (g) Be adequately documented. See also §§200.300 Statutory and national policy requirements through 200.309 Period of performance of this part.

Section 200.410 Collection of unallowable costs.

Payments made for costs determined to be unallowable by either the Federal awarding agency, cognizant agency for indirect costs, or pass-through entity, either as direct or indirect costs, must be refunded (including interest) to the Federal Government in accordance with instructions from the Federal agency that determined the costs are unallowable unless Federal statute or regulation directs otherwise. See also Subpart D— Post Federal Award Requirements of this part, §§200.300 Statutory and national policy requirements through 200.309 Period of performance.

Section 200.516 Audit findings, states in part:

- (a) *Audit findings reported.* The auditor must report the following as audit findings in a schedule of findings and questioned costs:
 - (3) Known questioned costs that are greater than \$25,000 for a type of compliance requirement for a major program. Known questioned costs are those specifically identified by the auditor. In evaluating the effect of questioned costs on the opinion on compliance, the auditor considers the best estimate of total costs questioned (likely questioned costs), not just the questioned costs specifically identified (known questioned costs). The auditor must also report known questioned costs when likely questioned costs are greater than \$25,000 for a type of compliance requirement for a major program. In reporting questioned costs, the auditor must include information to provide proper perspective for judging the prevalence and consequences of the questioned costs.

Title 42 U.S. Code of Federal Regulations Part 433, State Fiscal Administration, Subpart F – Refunding of Federal Share of Medicaid Overpayments to Providers

Section 433.300 Basis states in part:

This subpart implements -

- (a) Section 1903(d)(2)(A) of the Act, which directs that quarterly Federal payments to the States under title XIX (Medicaid) of the Act are to be reduced or increased to make adjustment for prior overpayments or underpayments that the Secretary determines have been made.
- (b) Section 1903(d)(2)(C) and (D) of the Act, which provides that a State has 1 year from discovery of an overpayment for Medicaid services to recover or attempt to

recover the overpayment from the provider before adjustment in the Federal Medicaid payment to the State is made; and that adjustment will be made at the end of the 1-year period, whether or not recovery is made, unless the State is unable to recover from a provider because the overpayment is a debt that has been discharged in bankruptcy or is otherwise uncollectable.

Title 45 U.S. Code of Federal Regulations Part 95, Subpart A - Time Limits for States To File Claims, states in part:

Section 95.7 Time limit for claiming payment for expenditures made after September 30, 1979 states:

Under the programs listed in § 95.1, we will pay a State for a State agency expenditure made after September 30, 1979, only if the State files a claim with us for that expenditure within 2 years after the calendar quarter in which the State agency made the expenditure. Section 95.19 lists the exceptions to this rule.

Section 95.19 Exceptions to time limits.

The time limits in §§ 95.7 and 95.10 do not apply to any of the following -

- (a) Any claim for an adjustment to prior year costs.
- (b) Any claim resulting from an audit exception.
- (c) Any claim resulting from a court-ordered retroactive payment.
- (d) Any claim for which the Secretary decides there was good cause for the State's not filing it within the time limit.

Office of Management and Budget OMB Uniform Guidance, Compliance Supplement for 2017, *Part 4 – Agency Program Requirements, 4.93.778 Medicaid Cluster*, states in part:

General Audit Approach for Medicaid Payments

To be allowable, Medicaid costs for medical services must be (1) covered by the State plan and waivers; (2) reviewed by the State consistent with the State's documented procedures and system for determining medical necessity of claims; (3) properly coded; and (4) paid at the rate allowed by the State plan. Additionally, Medicaid costs must be net of beneficiary cost-sharing obligations and applicable credits (e.g., insurance, recoveries from other third parties who are responsible for covering the Medicaid costs, and drug rebates), paid to eligible providers, and only provided on behalf of eligible individuals.

2018-046

The Health Care Authority did not have adequate internal controls over and did not comply with suspension and debarment requirements for Medicaid medical fee-for-service providers.

Federal Awarding Agency: U.S. Department of Health and Human Services
Pass-Through Entity: None
CFDA Number and Title: 93.775 State Medicaid Fraud Control Units
93.777 State Survey and Certification of Health Care Providers and Suppliers (Title XVIII) Medicare
93.778 Medical Assistance Program (Medicaid; Title XIX)
Federal Award Number: 1805WA5MAP; 1805WA5ADM; 1805WAIMPL; 1805WAINCT
Applicable Compliance Component: Suspension and Debarment
Known Questioned Cost Amount: None

Background

Medicaid is a jointly funded state and federal partnership providing coverage for about 1.9 million eligible low-income Washington residents who otherwise might go without medical care. Medicaid is Washington's largest public assistance program and accounts for about one-third of the State's federal expenditures. The program spent about \$12.7 billion in federal and state funds during fiscal year 2018.

Federal regulations prohibit grant recipients from contracting with or making subawards to parties suspended or debarred from doing business with the federal government. The grantee must verify that all contractors receiving \$25,000 or more in federal funds, or any subrecipients, have not been suspended or debarred or otherwise excluded. This verification may be accomplished by obtaining a written certification from the contractor or subrecipient or inserting a clause into the contract where the contractor or subrecipient states it is not suspended or debarred. Alternatively, the grantee may search the federal System For Award Management (SAM). This requirement must be met before entering into the contract.

The Medicaid program has additional requirements to ensure Medicaid providers are not suspended or debarred. Federal regulations require state Medicaid agencies to determine the exclusion status of providers and any person with an ownership or control interest or who is an agent or managing employee of the provider through routine checks of the List of Excluded Individuals/Entities (LEIE) and the Excluded Parties List System (EPLS). (In November 2012 the EPLS system was replaced with the System For Award and Management (SAM) database.)

The regulation requires state Medicaid agencies to perform LEIE and EPLS/SAM checks upon enrollment and re-enrollment of providers. For all enrolled providers, owners and managing employees, LEIE and EPLS/SAM checks must be completed at least monthly.

Over 96,000 Medicaid providers were active in Washington during fiscal year 2018. The Health Care Authority (Authority), which administers the state's Medicaid program, spent about \$1.45 billion for fee-for-service claims billed by medical providers.

In the prior audit, we reported the Authority did not have adequate internal controls over and did not comply with suspension and debarment requirements for Medicaid medical fee-for-service providers. The prior finding number was 2017-037.

Description of Condition

We found the Authority did not have adequate internal controls over and did not comply with suspension and debarment requirements for Medicaid medical fee-for-service providers.

The Authority performs LEIE and EPLS/SAM database checks upon enrollment and re-enrollment of medical fee-for-service providers. The Authority also performs the required monthly LEIE database checks. However, we found the Authority did not complete the required monthly EPLS/SAM database checks. The Authority did not perform EPLS/SAM checks for any months during our audit period.

We consider this internal control deficiency to be a material weakness.

Cause of Condition

The SAM database only has the ability to look up a single individual or an entity; therefore the Authority said it cannot complete data matches for all 96,000 providers monthly. The Authority is working with the federal government to resolve this issue.

Effect of Condition

We confirmed the Authority did not pay any debarred or suspended provider during the audit period. However, not conducting required monthly database checks in a timely manner increases the risk that the Authority would not detect and prevent suspended or debarred providers from receiving federal Medicaid funds. Payments to providers who are suspended or debarred would be unallowable, and the Authority could be required to repay the grantor for any such payments.

Recommendation

We recommend the Authority establish adequate internal controls to ensure it completes required EPLS/SAM checks at least monthly.

Authority's Response

As noted by the State Auditor's Office, the Authority conducts LEIE and EPLS database checks during the provider enrollment process for new enrollees and during re-validation.

The EPLS database checks are currently not conducted on a monthly basis by the Authority as there is a price associated with the SAM/EPLS database checks for an upload of more than one individual

provider at a time. The Authority has not had adequate staffing nor the budget to pay to have these checks conducted on a monthly basis due to the volume of its providers.

The Authority's work to utilize the U.S. Department of Treasury's Do Not Pay database system has stalled on the Federal side. The Authority is exploring other opportunities which will provide the capability to upload the high volume of providers into SAM/EPLS and conduct the required checks on a monthly basis.

Under the Authority's Apple Health contract, Managed Care Organizations (MCOs) are delegated to conduct the LEIE and SAM/EPLS database checks on network providers, which account for the majority of contracted providers. Per the contract requirements, MCOs report, to the Authority, any provider who appears in any of the databases and terminates the provider as necessary. The MCOs have been compliant with the aforementioned contract requirements which reduces the Authority's risk.

Although there is a current gap in the Authority's ability to conduct the SAM/EPLS database checks on a monthly basis, there were no improper payments identified.

Auditor's Concluding Remarks

We thank the Authority for its cooperation and assistance throughout the audit. We will review the status of the Authority's corrective action during our next audit.

Applicable Laws and Regulations

Title 2 U.S. Code of Federal Regulations Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance) establishes the following applicable requirements:

Section 200.303 Internal controls, states in part:

The non-Federal entity must:

- (a) Establish and maintain effective internal control over the Federal award that provides reasonable assurance that the non-Federal entity is managing the Federal award in compliance with Federal statutes, regulations, and the terms and conditions of the Federal award. These internal controls should be in compliance with guidance in "Standards for Internal Control in the Federal Government" issued by the Comptroller General of the United States or the "Internal Control Integrated Framework", issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).
- (b) Comply with Federal statutes, regulations, and the terms and conditions of the Federal awards.
- (d) Take prompt action when instances of noncompliance are identified including noncompliance identified in audit findings.

Section 200.516 Audit findings, states in part:

- (a) *Audit findings reported.* The auditor must report the following as audit findings in a schedule of findings and questioned costs:

- (1) Significant deficiencies and material weaknesses in internal control over major programs and significant instances of abuse relating to major programs. The auditor's determination of whether a deficiency in internal control is a significant deficiency or material weakness for the purpose of reporting an audit finding is in relation to a type of compliance requirement for a major program identified in the Compliance Supplement.
- (2) Material noncompliance with the provisions of Federal statutes, regulations, or the terms and conditions of Federal awards related to a major program. The auditor's determination of whether a noncompliance with the provisions of Federal statutes, regulations, or the terms and conditions of Federal awards is material for the purpose of reporting an audit finding is in relation to a type of compliance requirement for a major program identified in the compliance supplement.

The American Institute of Certified Public Accountants defines significant deficiencies and material weaknesses in internal controls over compliance in its *Codification of Statements on Auditing Standards*, section 935, Compliance Audits, as follows:

.11 For purposes of adapting GAAS to a compliance audit, the following terms have the meanings attributed as follows: ...

Deficiency in internal control over compliance. A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance on a timely basis. A deficiency in design exists when (a) a control necessary to meet the control objective is missing, or (b) an existing control is not properly designed so that, even if the control operates as designed, the control objective would not be met. A deficiency in operation exists when a properly designed control does not operate as designed or the person performing the control does not possess the necessary authority or competence to perform the control effectively.

Material weakness in internal control over compliance. A deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a compliance requirement will not be prevented, or detected and corrected, on a timely basis. In this section, a reasonable possibility exists when the likelihood of an event occurring is either reasonably possible or probable as defined as follows:

Reasonably possible. The chance of the future event or events occurring is more than remote but less than likely.

Probable. The future event or events are likely to occur.

Significant deficiency in internal control over compliance. A deficiency, or a combination of deficiencies, in internal control over compliance that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

Material noncompliance. In the absence of a definition of material noncompliance in the governmental audit requirement, a failure to follow compliance requirements or a violation of prohibitions included in the applicable compliance requirements that results in

noncompliance that is quantitatively or qualitatively material, either individually or when aggregated with other noncompliance, to the affected government program.

Title 2, U.S. Code of Federal Regulation, part 180, states in part:

Subpart B – Covered Transactions

A covered transactions is a nonprocurement or procurement transactions that is subject to the prohibitions of this part. It may be a transaction at –

- (a) The primary tier, between a Federal agency and a person (see appendix to this part); or
- (b) A lower tier, between a participant in a covered transaction and another person.

Subpart C–Responsibilities of Participants Regarding Transactions Doing Business With Other Persons

§180.300 What must I do before I enter into a covered transaction with another person at the next lower tier?

When you enter into a covered transaction with another person at the next lower tier, you must verify that the person with whom you intend to do business is not excluded or disqualified. You do this by:

- (a) Checking SAM Exclusions; or
- (b) Collecting a certification from that person; or
- (c) Adding a clause or condition to the covered transaction with that person.

Title 42 U.S. Code of Federal Regulations section 455 Subpart E – Provider Screening and Enrollment, states in part:

Section 455.436 Federal database checks

The State Medicaid agency must do all of the following:

- (a) Confirm the identity and determine the exclusion status of providers and any person with an ownership or control interest or who is an agent or managing employee
- (b) Check the Social Security Administration’s Death Master File, the National Plan and Provider Enumeration System (NPPES), the List of Excluded Individuals/Entities (LEIE), the Excluded parties List System (EPLS) and any such other databases as the Secretary may prescribe.
- (c) (1) Consult appropriate databases to confirm identity upon enrollment and reenrollment; and
(2) Check the LEIE and EPLS no less frequently than monthly.

2018-047 The Health Care Authority, Section of Program Integrity, Data Analytics and Review Unit, did not establish adequate internal controls over and did not comply with requirements to identify and refer suspected fraud cases for investigation.

Federal Awarding Agency: U.S. Department of Health and Human Services
Pass-Through Entity: None
CFDA Number and Title: 93.775 State Medicaid Fraud Control Units
93.777 State Survey and Certification of Health Care Providers and Suppliers (Title XVIII) Medicare
93.778 Medical Assistance Program (Medicaid; Title XIX)
Federal Award Number: 1805WA5MAP; 1805WA5ADM; 1805WAIMPL; 1805WAINCT
Applicable Compliance Component: Special Tests and Provisions – Utilization Control and Program Integrity
Known Questioned Cost Amount: None

Background

Medicaid is a jointly funded state and federal partnership providing coverage for about 1.9 million eligible low-income Washington residents who otherwise might go without medical care. Medicaid is Washington’s largest public assistance program and accounts for about one-third of the State’s federal expenditures. The program spent about \$12.7 billion in federal and state funds during fiscal year 2018.

Federal regulations require states to develop methods and criteria for identifying and investigating suspected fraud cases within the Medicaid program. In addition, the state Medicaid agency must develop procedures, in cooperation with State legal authorities, for referring suspected fraud cases to law enforcement officials, including the State Medicaid Fraud Control Unit (MFCU).

The Section of Program Integrity (Section) is the main office within the Health Care Authority (Authority) that performs program integrity reviews of Medicaid operations. The Section’s mission is to identify, prevent and recover improper payments to providers and its contractors, and identify noncompliance with state and federal regulations as well as with contractual requirements. This mission is carried out through:

- Data mining and analysis of payment transactions to identify potential fraud
- Conducting audits and reviews of health care providers, contractors, and subcontractors to ensure compliance with applicable laws and regulations
- Preventing future improper payments by recommending process improvements through amended program policies and Medicaid payment system edits
- Providing educational outreach to Medicaid providers, managed-care organizations, health care associations, and other Medicaid contractors to identify, report and prevent fraud

The Section's Data Analytics and Review Unit (Unit) is responsible for developing algorithms to detect and prevent fraud, waste and abuse; as well as identifying improperly paid claims, premiums and client benefits, and unusual provider billing practices; ensuring data integrity; and referring potential credible allegations of fraud. The Unit also conducts focused provider case reviews in which billing patterns by a particular provider (or group of providers) are analyzed to determine the likelihood of fraud.

During fiscal year 2018, the Data Analytics and Review Unit ran 15 algorithms to detect improper Medicaid payments and identify future cost avoidances. In addition, four Surveillance and Utilization Review Section (SURS) Analysts performed 37 provider case reviews to attempt to detect fraud.

In fiscal year 2018, the Authority processed \$51.6 million in improper payment recoveries, and identified an additional cost avoidance of \$28.2 million through system improvements, provider educational outreach, and revisions to contract and billing guide language. The state Medicaid program paid about \$6 million for program integrity operations at the Authority.

Description of Condition

The Authority did not have adequate internal controls over and did not comply with requirements to identify and refer suspected fraud cases for investigation.

Provider case reviews

The Unit did not have policies and procedures pertaining to algorithms and provider case reviews. Draft policies were created and implemented on March 14, 2018. The policies and procedures were officially signed on June 13, 2018.

We reviewed the Unit's policies and procedures and determined they do not address secondary reviews of analyst research to determine if the decision to report or not report the case to MFCU is substantiated. The Authority confirmed that no secondary reviews of provider case reviews were performed during the audit period.

We consider this control deficiency to be a material weakness.

This condition was not reported in the prior audit.

Cause of Condition

The Authority did not believe that secondary reviews of provider case reviews were necessary to ensure the analyst's findings were accurate and supported.

Unit management did not establish written policies and procedures when the Unit was created. The Unit became aware that policies and procedures were not documented and during the audit period took steps to implement written policies and procedures. The delay was caused by the need to gather input from stakeholders within the Authority.

The Unit did not set standards for documentation regarding analyst case work. Additionally, management did not review case notes to ensure all work performed by the analyst was adequately documented.

Effect of Condition

Provider case reviews

We used a non-statistical sampling method to randomly select and examine nine provider case reviews out of a total population of 37 cases completed during fiscal year 2018.

For seven of the nine cases (78 percent), we could not determine whether the reviews were completed in accordance with Unit policies and procedures because there was insufficient supporting documentation to substantiate the work performed by the SURS analyst assigned to the case. The documentation contained only the final decision arrived at by the SURS analyst, and in some cases, notations made by the analyst. However, these notations did not adequately document the type(s) of information that the SURS analyst reviewed to form their decision of a non-credible allegation of fraud.

By not requiring secondary reviews of provider cases opened by SURS analysts, the Authority has no assurance that all credible cases of fraud have been properly identified and referred to the State MFCU. Failure to identify all suspected fraud cases increases the risk of undetected improper payments within the Medicaid program.

Recommendations

We recommend the Authority:

- Monitor provider case reviews to ensure they are performed and documented in accordance with Unit policies and procedures. As part of its monitoring, we recommend the Authority implement a supervisory review of cases
- Require analysts to document the considerations they evaluated during provider case reviews when deciding whether to refer a case to the State MFCU

Authority's Response

The Authority disagrees with the statement made under Effect of Condition, "...the Authority has no assurance that all credible cases of fraud have been properly identified and referred to the State MFCU". Consistent with the Section's Case Management Policy and Case Management Team Charter, cases requiring further reviews were presented and reviewed by the Team to determine further action including investigation of suspected fraud and potential fraud referral to MFCU.

The Authority agrees with the findings of:

- *DAR Unit policies and procedures do not require a secondary review by the DAR manager. The Authority will implement changes to ensure secondary reviews are conducted; and*
- *Several cases did not have sufficient documentation in the case tracking system. The unit manager will ensure staff are properly trained and will conduct periodic reviews of documentation to ensure it follows Unit and Section documentation requirements.*

Auditor’s Concluding Remarks

We did not evaluate the effectiveness of the Authority’s Case Management Team reviews because the Authority did not provide evidence of Case Management Team meetings to review active and/or completed investigations for appropriateness. Therefore, we could not confirm the Authority ensured all credible cases of fraud or abuse were referred to the MFCU, as required.

We reaffirm our finding and we will review the status of the Authority’s corrective action during our next audit.

Applicable Laws and Regulations

Title 2 U.S. Code of Federal Regulations Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance) establishes the following applicable requirements:

Section 200.303 Internal controls, states in part:

The non-Federal entity must:

- (a) Establish and maintain effective internal control over the Federal award that provides reasonable assurance that the non-Federal entity is managing the Federal award in compliance with Federal statutes, regulations, and the terms and conditions of the Federal award. These internal controls should be in compliance with guidance in “Standards for Internal Control in the Federal Government” issued by the Comptroller General of the United States or the “Internal Control Integrated Framework”, issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).
- (b) Comply with Federal statutes, regulations, and the terms and conditions of the Federal awards.
- (d) Take prompt action when instances of noncompliance are identified including noncompliance identified in audit findings.

Section 200.516 Audit findings, states in part:

- (a) *Audit findings reported.* The auditor must report the following as audit findings in a schedule of findings and questioned costs:
 - (1) Significant deficiencies and material weaknesses in internal control over major programs and significant instances of abuse relating to major programs. The auditor’s determination of whether a deficiency in internal control is a significant deficiency or material weakness for the purpose of reporting an audit finding is in relation to a type of compliance requirement for a major program identified in the Compliance Supplement.
 - (2) Material noncompliance with the provisions of Federal statutes, regulations, or the terms and conditions of Federal awards related to a major program. The auditor’s determination of whether a noncompliance with the provisions of Federal statutes, regulations, or the terms and conditions of Federal awards is material for the purpose of reporting an audit finding is in relation to a type of compliance requirement for a major program identified in the compliance supplement.

The American Institute of Certified Public Accountants defines significant deficiencies and material weaknesses in internal controls over compliance in its *Codification of Statements on Auditing Standards*, section 935, Compliance Audits, as follows:

.11 For purposes of adapting GAAS to a compliance audit, the following terms have the meanings attributed as follows: ...

Deficiency in internal control over compliance. A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance on a timely basis. A deficiency in design exists when (a) a control necessary to meet the control objective is missing, or (b) an existing control is not properly designed so that, even if the control operates as designed, the control objective would not be met. A deficiency in operation exists when a properly designed control does not operate as designed or the person performing the control does not possess the necessary authority or competence to perform the control effectively.

Material weakness in internal control over compliance. A deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a compliance requirement will not be prevented, or detected and corrected, on a timely basis. In this section, a reasonable possibility exists when the likelihood of an event occurring is either reasonably possible or probable as defined as follows:

Reasonably possible. The chance of the future event or events occurring is more than remote but less than likely.

Probable. The future event or events are likely to occur.

Significant deficiency in internal control over compliance. A deficiency, or a combination of deficiencies, in internal control over compliance that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

Material noncompliance. In the absence of a definition of material noncompliance in the governmental audit requirement, a failure to follow compliance requirements or a violation of prohibitions included in the applicable compliance requirements that results in noncompliance that is quantitatively or qualitatively material, either individually or when aggregated with other noncompliance, to the affected government program.

Title 42 U.S. Code of Federal Regulations Part 455, Program Integrity: Medicaid, Subpart A – Medicaid Agency Fraud Detection and Investigation Program, states in part:

455.13. Methods for identification, investigation, and referral.

The Medicaid agency must have –

- (a) Methods and criteria for identifying suspected fraud cases;
- (b) Methods for investigating these cases that –
 - (1) Do not infringe on the legal rights of persons involved; and
 - (2) Afford due process of law; and
- (c) Procedures, developed in cooperation with State legal authorities, for referring suspected fraud cases to law enforcement officials.

455.14. Preliminary investigation.

If the agency receives a complaint of Medicaid fraud or abuse from any source or identifies any questionable practices, it must conduct a preliminary investigation to determine whether there is sufficient basis to warrant a full investigation.

455.15. Full investigation.

If the findings of a preliminary investigation give the agency reason to believe that an incident of fraud or abuse has occurred in the Medicaid program, the agency must take the following action, as appropriate:

- (a) If a provider is suspected of fraud or abuse, the agency must –
 - (1) In States with a State Medicaid fraud control unit certified under subpart C of part 1002 of this title, refer the case to the unit under the terms of its agreement with the unit entered into under § 1002.309 of this title;
- (b) If there is reason to believe that a beneficiary has defrauded the Medicaid program, the agency must refer the case to an appropriate law enforcement agency.
- (c) If there is reason to believe that a beneficiary has abused the Medicaid program, the agency must conduct a full investigation of the abuse.

455.16. Resolution of full investigation.

A full investigation must continue until –

- (a) Appropriate legal action is initiated;
- (b) The case is closed or dropped because of insufficient evidence to support the allegations of fraud or abuse; or
- (c) The matter is resolved between the agency and the provider or beneficiary. This resolution may include but is not limited to –
 - (1) Sending a warning letter to the provider or beneficiary, giving notice that continuation of the activity in question will result in further action;
 - (2) Suspending or terminating the provider from participation in the Medicaid program;
 - (3) Seeking recovery of payments made to the provider; or
 - (4) Imposing other sanctions provided under the State plan.

Title 42 U.S. Code of Federal Regulations Part 456, Utilization Control, Subpart A – General Provisions, states in part:

456.1. Basis and purpose of part.

- (b) The requirements in this part are based on the following sections of the Act. Table 1 shows the relationship between these sections of the Act and the requirements in this part.
 - (1) *Methods and procedures to safeguard against utilization of care and services.* Section 1902(a)(30) requires that the State plan provide methods and procedures to safeguard against unnecessary utilization of care and services.

456.2. State plan requirements.

- (a) A State plan must provide that the requirements of this part are met.
- (b) These requirements may be met by the agency by:
 - (1) Assuming direct responsibility for assuring that the requirements of this part are met;

456.3. Statewide surveillance and utilization control program.

The Medicaid agency must implement a statewide surveillance and utilization control program that –

- (a) Safeguards against unnecessary or inappropriate use of Medicaid services and against excess payments;
- (b) Assesses the quality of those services;
- (c) Provides for the control of the utilization of all services provided under the plan in accordance with subpart B of this part; and
- (d) Provides for the control of the utilization of inpatient services in accordance with subparts C through I of this part.

456.4. Responsibility for monitoring the utilization control program.

- (a) The agency must –
 - (1) Monitor the statewide utilization control program;
 - (2) Take all necessary corrective action to ensure the effectiveness of the program;
 - (3) Establish methods and procedures to implement this section;
 - (4) Keep copies of these methods and procedures on file; and
 - (5) Give copies of these methods and procedures to all staff involved in carrying out the utilization control program.

456.5. Evaluation criteria.

The agency must establish and use written criteria for evaluating the appropriateness and quality of Medicaid services.

Title 42 U.S. Code of Federal Regulations Part 456, Utilization Control, Subpart B – Utilization Control: All Medicaid Services, states in part:

456.23 – Post-payment review process.

The agency must have a post-payment review process that –

- (a) Allows State personnel to develop and review –
 - (1) Beneficiary utilization profiles;
 - (2) Provider service profiles; and
 - (3) Exceptions criteria; and
- (b) Identifies exceptions so that the agency can correct misutilization practices of beneficiaries and providers.

The Washington State Plan under Title XIX of the Social Security Act – Medical Assistance Program, Section 4.5 – Medicaid Agency Fraud Detection and Investigation Program, states:

The Medicaid agency has established and will maintain methods, criteria, and procedures that meet all requirements of 42 CFR 455.13 through 455.21, and 455.23 for prevention and control of program fraud and abuse.

Washington Administrative Code, 182-502A-0401 *Program integrity activities*, states in part:

1. Form. Program integrity activities include:
 - (a) Conducting audits;
 - (b) Conducting reviews;
 - (c) Conducting investigations;
 - (d) Initiating and reviewing entity self-audits under WAC 182-502A-0501;
 - (e) Applying algorithms to claim or encounter data;
 - (f) Conducting on-site inspections of entity locations; and
 - (g) Verifying entity compliance with applicable laws, rules, regulations, and agreements.
5. Scope. The agency determines the scope of a program integrity activity.
6. Selecting information to evaluate.
 - (a) The agency may evaluate any information relevant to validating that the payee received only those funds to which it is legally entitled. In this chapter, “relevant” has a meaning identical to Federal Rule of Evidence 401.
 - (b) The agency may select information to evaluate by:
 - (i) Conducting a risk assessment of claim or encounter data;
 - (ii) Applying algorithms;
 - (iii) Data mining;
 - (iv) Claim-by-claim review;
 - (v) Encounter-by-encounter review;
 - (vi) Stratified random sampling;
 - (vii) Nonstratified random sampling; or
 - (viii) Applying any other method, or combination of methods, designed to identify relevant information.
8. Evaluating information.
 - (a) The agency may evaluate relevant information by applying any method or combination of methods reasonably calculated to determine whether an entity has complied with an applicable law, regulation or agreement.
 - (b) A health care provider’s bill for services, appointment books, accounting records, or other similar documents alone do not qualify as appropriate documentation of services rendered.
 - (c) The agency provides the entity a description of the method or combination of methods used by the agency under subsection (6) of this section.

The Washington Health Care Authority, Section of Program Integrity (PI), Data Analytics & Review (DAR) Policy Manual, Chapter 4: Provider Case Review, No. 4-0 states:

PURPOSE

The purpose of this policy is to ensure that DAR has explicit policy governing case work so that staff completes all cases in the most appropriate way relevant to the matter under investigation.

BACKGROUND

Per 42 CFR Part 455, HCA must conduct a preliminary investigation of every complaint of Medicaid fraud or abuse and every questionable practice it identifies. HCA conducts data analysis to identify questionable practices under Part 456. Part 455 also requires HCA to conduct a full investigation when a preliminary investigation gives the agency reason to believe an incident of fraud or abuse has occurred. The case work must continue until each full investigation is resolved.

POLICY REQUIREMENTS

1. All DAR staff conducting case work must abide by the policies and procedures that govern case work.
2. In addition, successful case work is a community effort. DAR staff will provide mutual support. This policy encourages the investigator to seek assistance from agency subject matter experts.

The Washington Health Care Authority, Section of Program Integrity (PI), Data Analytics & Review (DAR) Procedure Manual, Chapter 4: Provider Case Review, No. 4-0-01 states:

Procedure

Leads are generated by a variety of sources including but not limited to SME Peer Profiling activity, HotTips, Program Managers and sources inside and outside the agency. Leads generated through the In-take process are assigned to the appropriate SME for preliminary triage. The SME determines (on case by case basis) whether or not to enter into the tracking system or return to in-take. If the source of the lead is a Medical Service Verification (MSV) follow the MSV process.

Action by DAR Staff:

1. Enter provider information directly into tracking system and open as Preliminary Investigation Assessed for:

Appropriateness

Jurisdiction. Some matters are not the appropriate for DAR SURS review such as welfare fraud and quality of care.

Sufficiency

To be sufficient a lead must at least have a clear allegation and identify the alleged perpetrator.

Generally, a complaint is insufficient when it provides too little information to specify the perpetrator. However, a complaint may be sufficient when it identifies a material problem of a general nature, such as improper claims processing that is not specific to a perpetrator.

A complaint is insufficient when the allegation fails to define the allegation.

Significance

The potential for monetary loss and for recovery are the usual measures of significance. The greater the financial risk the higher the significance. Likewise, matters of high media profile or potential infamy are deemed of significance relative to the degree of notoriety. DAR staff Unit alerts SPI management to such matters immediately.

Credibility

Information used to evaluate leads have varying levels of credibility. The following are examples of situations of relatively high credibility:

- Information developed during prepayment and post-payment review of medical records.
- Data analysis that shows the provider's utilization to be well above that of its peers without any apparent legitimate rationale.
- Billing patterns so aberrant from the norm that they bring into question the correctness of the payments made.
- Allegations that items or services were not furnished or received as billed. Documented allegations have higher credibility than undocumented allegations.
- Allegations of false billing from a provider's employees.
- Evidence of aberrant billing practices reported by staff monitoring and/or processing claims and matters related to authorizations.
- Eye witness accounts by clients and/or a provider's peers.

Credibility depends upon the source (i.e. may include but not limited to):

- Clients and/or their families;
- Provider employees and similar professionals
- WA Dept. of Social and Health Services employees
- Health Care Authority employees
- Department of Health (DOH)
- Professional licensing and facility credentialing agencies
- Centers for Medicare and Medicaid Services (CMS)
- Office of the Inspector General (OIG)
- U.S. Department of Justice (DOJ)
- Federal Bureau of Investigation (FBI)
- U.S. Attorney and state and local law enforcement
- Other governing agencies

1. Based on risk/findings determine how the case will proceed:

a. Close the case using the appropriate disposition (below)

Administration advised not to pursue: This means that legitimate supervisory authority told HCA not to pursue a case. This is not a common occurrence. An example would be direction from the Office of the US Attorney to 'stand down' so as not to interfere with federal action. Another would be direction from the Governor's Office not to pursue a case.

Insufficient findings to substantiate a full review at this time: This disposition is used in cases where there is suspicion yet the evidence is negligible and/or unsubstantiated

to identify a clear wrongful act, AND continued monitoring is prudent AND the analyst determines future follow-up should be scheduled. Close the case using the “tickler” function to set a reminder; follow-up increments of 4 months is advised.

Lacks materiality to warrant review at this time: PI Management determined that it is not cost effective to investigate providers that have received payment less than \$5,000 annually for consecutive years. The exception is evidence of suspected fraudulent activity.

No further action by this section is appropriate: If this option is selected, one must enter comprehensive notes. This may be closed “delivered provider education.”

Opened in error: This may be used when the case was opened inadvertently more than once, the unit designation is not accurate, it’s an MVS and the form is incomplete and should not have been opened or it was opened using misinformation. Always clearly document the reasons the case was opened in error in the note screen. Never use this option to close a case that was opened and triage indicated there was insufficient evidence or data to merit review.

Open Full Scale Investigation: Case requires referral, additional documents to substantiate payments such as evidence from provider, client, or other state agency etc.

2. Full Scale Investigation: Is a comprehensive investigation that requires compilation of organized evidence. These tasks include but are not limited to:
 - a. Understand the Provider Case Review Checklist
 - b. Review provider history with governing agencies
 - c. Identify all provider numbers and affiliations
 - d. Understand contracted requirements of CPA.
3. Refer for follow-up outside the unit: based on findings determine if a referral is required. If so refer to the appropriate entity, discuss the referral with appropriate staff at the referral destination. Comply with specific processes i.e. submit forms and obtain approval as required and refer to one of the options in the case tracking system.
4. Based on risk/findings determine how the case will proceed and close with appropriate disposition.

2018-048

The Health Care Authority did not have adequate internal controls over and did not comply with requirements to ensure Medicaid expenditures were allowable to claim Children’s Health Insurance Program funds.

Federal Awarding Agency: U.S. Department of Health and Human Services
Pass-Through Entity: None
CFDA Number and Title: 93.775 State Medicaid Fraud Control Units
93.777 State Survey and Certification of Health Care Providers and Suppliers (Title XVIII) Medicare
93.778 Medical Assistance Program (Medicaid; Title XIX)
Federal Award Number: 1805WA5MAP; 1805WA5ADM; 1805WAIMPL; 1805WAINCT
Applicable Compliance Component: Activities Allowed/Unallowed Allowable Costs/Cost Principles
Known Questioned Cost Amount: \$4,145

Background

Medicaid is a jointly funded state and federal partnership providing coverage for about 1.9 million eligible low-income Washington residents who otherwise might go without medical care. Medicaid is Washington’s largest public assistance program and accounts for about one-third of the State’s federal expenditures. The program spent about \$12.7 billion in federal and state funds during fiscal year 2018.

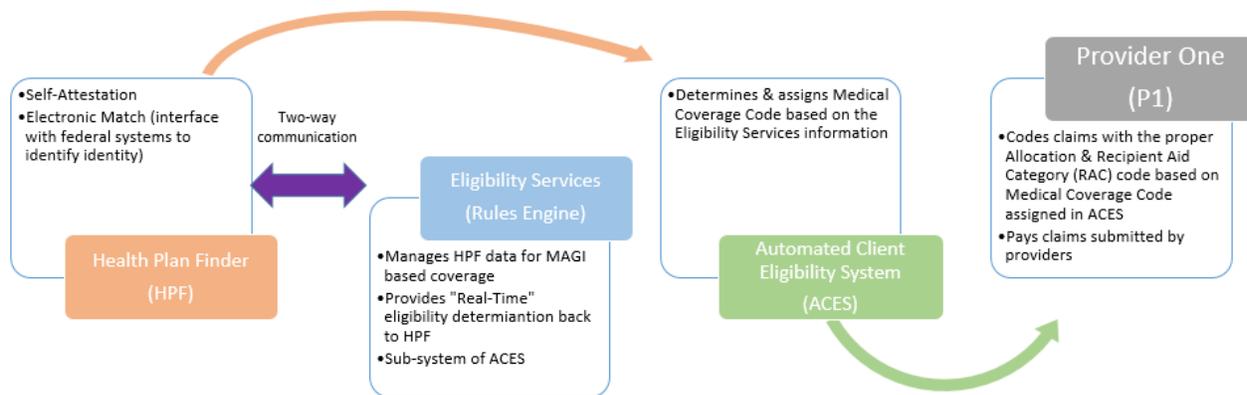
In fiscal year 2018, the state Medicaid program paid about \$437 million for Medicaid eligible children under 42 U.S. Code §1397ee authority.

In Washington, Medicaid and the CHIP program provide medical and behavioral health assistance for children up to 19 years old who reside in low-income households. Both programs are funded by State and federal money. Federal funds reimburse the State for about 88 percent of CHIP expenditures and 50 percent of Medicaid expenditures incurred by the Health Care Authority (Authority).

The State may claim additional CHIP funding when two conditions are met: a child is younger than 19 at the time of service and the child’s family income equals or exceeds 133 percent of the federal poverty level, but does not exceed the Medicaid applicable income level (which is 210 percent of the federal poverty level). If the Medicaid costs have already been claimed and reimbursed, the State submits a claim for the difference between the CHIP and Medicaid rates.

The following describes the process the Authority uses to identify Medicaid expenditures that are allowable for the additional CHIP funds:

- Medicaid eligibility is determined in the Eligibility Services system based on income information submitted by applicants through Health Plan Finder, www.wahealthplanfinder.org, the online application system (see diagram below).
- The Eligibility Service then notifies ProviderOne, the Authority’s Medicaid Management Information System, of the appropriate Recipient Aid Category (RAC) code for the children who are eligible for additional CHIP funds based on income information in the Automated Client Eligibility System (Eligibility System), Washington’s social service program client eligibility system.
- The Authority creates a report showing all payments that ProviderOne assigns both a RAC code of 1204 and an allocation code of 3MXA; payments that are assigned both these codes are identified as allowable for additional CHIP funding.



The Authority uses ProviderOne to identify Medicaid expenditures and prepare a journal voucher based on the RAC and allocations to identify allowable Medicaid expenditures.

In prior audits, we reported the Authority did not have adequate internal controls to ensure additional CHIP funds were properly claimed for allowable Medicaid expenditures. The prior finding numbers were 2017-038, 2016-034, 2015-039, and 2014-037. Prior findings reported inadequate internal controls over additional CHIP funds for the Authority’s fee-for service and managed care claims.

Description of Condition

The Authority did not have adequate internal controls over and did not comply with requirements to ensure Medicaid expenditures were allowable to claim CHIP funds.

The Authority performs a post-eligibility review on required programs as outlined in the state’s verification plan to ensure Medicaid eligibility is properly determined.

However, it performs the review only when household income is above the Medicaid applicable income level. The applicable family income for Medicaid children is 210 percent of the federal poverty level. Additional CHIP funds are allowable for Medicaid children whose household income equals or exceeds

133 percent of the federal poverty level, but does not exceed 210 percent of that level. When a household's income is below 133 percent of the federal poverty level, the Authority does not conduct a post-eligibility review for Children's coverage.

Because the Authority did not perform post eligibility reviews for clients whose income was below 133 percent, it did not detect when RAC codes were incorrectly assigned to clients. This resulted in the Authority improperly claiming additional CHIP funds.

We used a statistical sampling method to randomly select and examine 86 clients of a total population of 242,835 who had a RAC code of 1204 and had paid fee-for-service and managed care claims with an allocation code of 3MXA during the period the claim was made for. We reviewed claims to determine if the Authority properly coded the clients and the claims as allowable for additional CHIP federal funds. We identified 17 claims that were not coded to the correct RAC and allocation code when the client's eligibility was determined for CHIP:

- 14 (16.3 percent) clients with income below 133 percent of the federal poverty level did not have the appropriate RAC code assigned at the time of service.
- Three (3.5 percent) clients with income above 210 percent of the federal poverty level did not have the appropriate RAC code assigned at the time of service. These clients should have been enrolled in the CHIP program, not the Medicaid program.

We consider this internal control deficiency to be a material weakness.

Cause of Condition

The Authority uses specific client eligibility criteria to determine claims that are allowable for additional CHIP federal funding. Clients attest to household income at the time of application. The Eligibility System determines client eligibility based on the first self-attested income that is entered, which is then coded to help identify within ProviderOne if the claim is allowable for additional CHIP federal funds. However, the Eligibility System does not re-determine eligibility of the client if changes to the household income is subsequently entered.

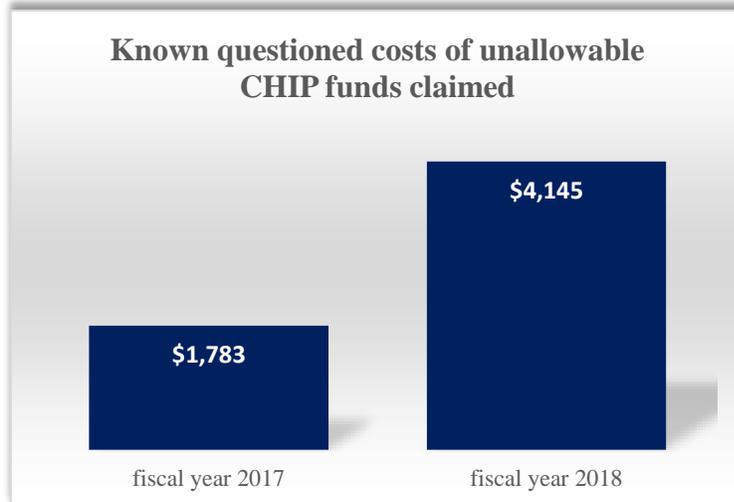
The Eligibility System is configured to accept changes to self-attested household income in Health Plan Finder during the certification period, but it is not updated to adequately determine eligibility for additional CHIP federal funds.

While the Authority fixed the previously identified issues around RAC assignment to ProviderOne in July 2017 the journal vouchers that were processed during the audit period included claims that were paid before the solution was implemented. For clients tested, eligibility determinations made after July 2017 were accurately determined and did not result in question costs.

The post-eligibility review is not designed to capture updates to household income when it falls below 133 percent of the federal poverty level, making those claims unallowable for the additional CHIPS funds.

Effect of Condition and Questioned Costs

We used a statistical sampling method to randomly select and examine 86 clients of a total population of 242,835 who had a RAC code of 1204 and had paid fee-for-service and managed care claims with an allocation code of 3MXA during the period the claim was made for. We reviewed each client’s federal poverty level and age at the time of service to determine if the claim was allowable for the additional CHIP match.



We found that for 14 clients, claims of \$3,293 in additional CHIP federal funds were unallowable. Additionally, we found that for three clients, claims of \$852 should have been charged to the CHIP grant because they were not eligible for Medicaid.

When we project the results to the entire population of Authority claims, we estimate the total improper payments to be

\$12,053,321.

Known questioned costs for fiscal year 2018 increased from \$1,783 to \$4,145 due to the increased amount of additional CHIP claims submitted during the year. In fiscal year 2017, the Authority was unsure of the status of the CHIP program and maintained a conservative approach when it drew down additional CHIP funds.

Projection to population	Known questioned costs – federal share*	Likely improper payments – federal share*
Claims not allowable for additional CHIP funds	\$3,293	\$9,778,900
Claims not allowable for Medicaid funds	\$852	\$2,274,421
Total expenditures	\$4,145	\$12,053,321

*Note: CHIP claims do not have a State match

Our sampling methodology meets statistical sampling criteria under generally accepted auditing standards in AU-C 530.05. It is important to note that the sampling technique we used is intended to support our audit conclusions by determining if expenditures complied with program requirements in all material respects. Accordingly, we used an acceptance sampling formula designed to provide a high level of assurance, with a 95 percent confidence of whether exceptions exceeded our materiality threshold. Our audit report and finding reflects this conclusion. However, the likely improper payment projections are a point estimate and only represent our “best estimate of total questioned costs” as required by 2 CFR 200.516(3). To ensure a representative sample, we stratified the population by dollar amount.

Recommendations

We recommend the Authority:

- Continue to implement procedures to ensure additional CHIP funds are claimed only for eligible expenditures
- Consult with the U.S. Department of Health and Human Services to discuss whether the questioned costs and improper payments identified in the audit should be repaid

Authority's Response

The Authority does not agree with the SAO's Description of Condition, Cause of Condition, Effect of Condition, or the estimated amount of improper payments. The Authority agrees with the actual questioned cost amount of \$3,293.

The questioned costs were due to a system issue identified during the 2016 audit. Certain RAC codes were not updating in ProviderOne when specific elements were missing during the annual renewal process. This RAC assignment issue was corrected in July of 2017. We appreciate that the SAO is required to question the costs identified since the correction occurred after the beginning of the audit period (July 1, 2017).

The Authority is concerned that the SAO may not have an understanding of the program sufficient to accurately assess the control structure. While the Authority agrees there were some ineligible costs, the cause of those instances was not due to PERs not being conducted as required and approved by CMS.

The Authority will consult with its grantor to resolve the \$4,145 in unallowable charges.

Auditor's Concluding Remarks

During our fieldwork, we confirmed the Authority did not have a monitoring or review process to ensure it only claimed CHIP funds for allowable Medicaid payments made for eligible children. In addition to a system error which incorrectly assigned the RAC codes to ineligible clients, the lack of monitoring resulted in the Authority claiming CHIP funds for unallowable Medicaid payments.

We reaffirm our finding and will review the status of the Authority's corrective action during our next audit.

Applicable Laws and Regulations

Title 2 U.S. Code of Federal Regulations Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance) establishes the following applicable requirements:

Section 200.53 Improper Payments states:

- (a) *Improper payment* means any payment that should not have been made or that was made in an incorrect amount (including overpayments and underpayments) under statutory, contractual, administrative, or other legally applicable requirements; and
- (b) *Improper payment* includes any payment to an ineligible party, any payment for an ineligible good or service, any duplicate payment, any payment for a good or service not received (except for such payments where authorized by law), any payment that does not account for credit for applicable discounts, and any payment where insufficient or lack of documentation prevents a reviewer from discerning whether a payment was proper.

Section 200.303 Internal controls, states in part:

The non-Federal entity must:

- (a) Establish and maintain effective internal control over the Federal award that provides reasonable assurance that the non-Federal entity is managing the Federal award in compliance with Federal statutes, regulations, and the terms and conditions of the Federal award. These internal controls should be in compliance with guidance in “Standards for Internal Control in the Federal Government” issued by the Comptroller General of the United States or the “Internal Control Integrated Framework”, issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).
- (b) Comply with Federal statutes, regulations, and the terms and conditions of the Federal awards.
- (d) Take prompt action when instances of noncompliance are identified including noncompliance identified in audit findings.

Section 200.403 Factors affecting Allowability of costs.

Except where otherwise authorized by statute, costs must meet the following general criteria in order to be allowable under Federal awards.

- (a) Be necessary and reasonable for the performance of the Federal award and be allocable thereto under these principles.
- (b) Conform to any limitations or exclusions set forth in these principles or in the Federal award as to types or amount of cost items.
- (c) Be consistent with policies and procedures that apply uniformly to both federally-financed and other activities of the non-Federal entity.
- (d) Be accorded consistent treatment. A cost may not be assigned to a Federal award as a direct cost if any other cost incurred for the same purpose in like circumstances has been allocated to the Federal award as an indirect cost.
- (e) Be determined in accordance with generally accepted accounting principles (GAAP), except, for state and local governments and Indian tribes only, as otherwise provided for in this part.
- (f) Not be included as a cost or used to meet cost sharing or matching requirements of any other federally-financed program in either the current or a prior period. See also §200.306 Cost sharing or matching paragraph (b).
- (g) Be adequately documented. See also §§200.300 Statutory and national policy requirements through 200.309 Period of performance of this part.

Section 200.410 Collection of unallowable costs.

Payments made for costs determined to be unallowable by either the Federal awarding agency, cognizant agency for indirect costs, or pass-through entity, either as direct or indirect costs, must be refunded (including interest) to the Federal Government in accordance with instructions from the Federal agency that determined the costs are unallowable unless Federal statute or regulation directs otherwise. See also Subpart D— Post Federal Award Requirements of this part, §§200.300 Statutory and national policy requirements through 200.309 Period of performance.

Section 200.516 Audit findings, states in part:

- (a) *Audit findings reported.* The auditor must report the following as audit findings in a schedule of findings and questioned costs:
- (1) Significant deficiencies and material weaknesses in internal control over major programs and significant instances of abuse relating to major programs. The auditor's determination of whether a deficiency in internal control is a significant deficiency or material weakness for the purpose of reporting an audit finding is in relation to a type of compliance requirement for a major program identified in the Compliance Supplement.
 - (2) Material noncompliance with the provisions of Federal statutes, regulations, or the terms and conditions of Federal awards related to a major program. The auditor's determination of whether a noncompliance with the provisions of Federal statutes, regulations, or the terms and conditions of Federal awards is material for the purpose of reporting an audit finding is in relation to a type of compliance requirement for a major program identified in the compliance supplement.
 - (3) Known questioned costs that are greater than \$25,000 for a type of compliance requirement for a major program. Known questioned costs are those specifically identified by the auditor. In evaluating the effect of questioned costs on the opinion on compliance, the auditor considers the best estimate of total costs questioned (likely questioned costs), not just the questioned costs specifically identified (known questioned costs). The auditor must also report known questioned costs when likely questioned costs are greater than \$25,000 for a type of compliance requirement for a major program. In reporting questioned costs, the auditor must include information to provide proper perspective for judging the prevalence and consequences of the questioned costs.

The American Institute of Certified Public Accountants defines significant deficiencies and material weaknesses in internal controls over compliance in its *Codification of Statements on Auditing Standards*, section 935, Compliance Audits, as follows:

- .11 For purposes of adapting GAAS to a compliance audit, the following terms have the meanings attributed as follows: ...

Deficiency in internal control over compliance. A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance on a timely basis. A deficiency in design

exists when (a) a control necessary to meet the control objective is missing, or (b) an existing control is not properly designed so that, even if the control operates as designed, the control objective would not be met. A deficiency in operation exists when a properly designed control does not operate as designed or the person performing the control does not possess the necessary authority or competence to perform the control effectively.

Material weakness in internal control over compliance. A deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a compliance requirement will not be prevented, or detected and corrected, on a timely basis. In this section, a reasonable possibility exists when the likelihood of an event occurring is either reasonably possible or probable as defined as follows:

Reasonably possible. The chance of the future event or events occurring is more than remote but less than likely.

Probable. The future event or events are likely to occur.

Significant deficiency in internal control over compliance. A deficiency, or a combination of deficiencies, in internal control over compliance that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

Material noncompliance. In the absence of a definition of material noncompliance in the governmental audit requirement, a failure to follow compliance requirements or a violation of prohibitions included in the applicable compliance requirements that results in noncompliance that is quantitatively or qualitatively material, either individually or when aggregated with other noncompliance, to the affected government program.

Office of Management and Budget OMB Uniform Guidance, Compliance Supplement for 2017, *Part 4 – Agency Program Requirements, 4.93.778 Medicaid Cluster*, states in part:

General Audit Approach for Medicaid Payments

To be allowable, Medicaid costs for medical services must be (1) covered by the State plan and waivers; (2) reviewed by the State consistent with the State’s documented procedures and system for determining medical necessity of claims; (3) properly coded; and (4) paid at the rate allowed by the State plan. Additionally, Medicaid costs must be net of beneficiary cost-sharing obligations and applicable credits (e.g., insurance, recoveries from other third parties who are responsible for covering the Medicaid costs, and drug rebates), paid to eligible providers, and only provided on behalf of eligible individuals.

42 U.S. Code §1397ee. Payments to States, states in part:

(g) Authority for qualifying states to use certain funds for Medicaid expenditures. -

(1) State option.—

(A) In general.—Notwithstanding any other provision of law subject to paragraph (4), a qualifying State (as defined in paragraph (2)) may elect to use not more than 20 percent of any allotment under section 1397dd of this title for fiscal year 1998, 1999, 2000, 2001, 2004, 2005, 2006, 2007, or 2008 (insofar as it is available under subsections (e) and (g) of such section) for payments under subchapter XIX of this

chapter in accordance with subparagraph (B), instead of for expenditures under this subchapter .

(B) Payments to states.—

(i) In general.—In the case of a qualifying State that has elected the option described in subparagraph (A), subject to the availability of funds under such subparagraph with respect to the State, the Secretary shall pay the State an amount each quarter equal to the additional amount that would have been paid to the State under subchapter XIX of this chapter with respect to expenditures described in clause (ii) if the enhanced FMAP (as determined under subsection (b) of this section) had been substituted for the Federal medical assistance percentage (as defined in section 1396d(b) of this title).

(ii) Expenditures described.—For purposes of this subparagraph, the expenditures described in this clause are expenditures, made after August 15, 2003, and during the period in which funds are available to the qualifying State for use under subparagraph (A), for medical assistance under subchapter XIX of this chapter to individuals who have not attained age 19 and whose family income exceeds 150 percent of the poverty line.

(iii) No impact on determination of budget neutrality for waivers.—In the case of a qualifying State that uses amounts paid under this subsection for expenditures described in clause (ii) that are incurred under a waiver approved for the State, any budget neutrality determinations with respect to such waiver shall be determined without regard to such amounts paid.

(2) Qualifying state.—In this subsection, the term “qualifying State” means a State that, on and after April 15, 1997, has an income eligibility standard that is at least 184 percent of the poverty line with respect to any 1 or more categories of children (other than infants) who are eligible for medical assistance under section 1396a(a)(10)(A) of this title or, in the case of a State that has a statewide waiver in effect under section 1315 of this title with respect to subchapter XIX of this chapter that was first implemented on August 1, 1994, or July 1, 1995, has an income eligibility standard under such waiver for children that is at least 185 percent of the poverty line, or, in the case of a State that has a statewide waiver in effect under section 1315 of this title with respect to subchapter XIX of this chapter that was first implemented on January 1, 1994, has an income eligibility standard under such waiver for children who lack health insurance that is at least 185 percent of the poverty line, or, in the case of a State that had a statewide waiver in effect under section 1315 of this title with respect to subchapter XIX of this chapter that was first implemented on October 1, 1993, had an income eligibility standard under such waiver for children that was at least 185 percent of the poverty line and on and after July 1, 1998, has an income eligibility standard for children under section 1396a(a)(10)(A) of this title or a statewide waiver in effect under section 1315 of this title with respect to subchapter XIX of this chapter that is at least 185 percent of the poverty line.

(3) Construction.—Nothing in paragraphs (1) and (2) shall be construed as modifying the requirements applicable to States implementing State child health plans under this subchapter.

(4) Option for allotments for fiscal years 2009 through 2015.—

- (A) Payment of enhanced portion of matching rate for certain expenditures.—In the case of expenditures described in subparagraph (B), a qualifying State (as defined in paragraph (2)) may elect to be paid from the State’s allotment made under section 1397dd of this title for any of fiscal years 2009 through 2015 (insofar as the allotment is available to the State under subsections (e) and (m) of such section) an amount each quarter equal to the additional amount that would have been paid to the State under subchapter XIX with respect to such expenditures if the enhanced FMAP (as determined under subsection (b)) had been substituted for the Federal medical assistance percentage (as defined in section 1396d(b) of this title).
- (B) Expenditures described.—For purposes graph (A), the expenditures described in this subparagraph are expenditures made after February 4, 2009, and during the period in which funds are available to the qualifying State for use under subparagraph (A), for the provision of medical assistance to individuals residing in the State who are eligible for medical assistance under the State plan under subchapter XIX or under a waiver of such plan and who have not attained age 19 (or, if a State has so elected under the State plan under subchapter XIX, age 20 or 21), and whose family income equals or exceeds 133 percent of the poverty line but does not exceed the Medicaid applicable income level.

2018-049 The Health Care Authority made improper payments for Medicaid managed care recipients with Medicare insurance coverage.

Federal Awarding Agency: U.S. Department of Health and Human Services
Pass-Through Entity: None
CFDA Number and Title: 93.775 State Medicaid Fraud Control Units
93.777 State Survey and Certification of Health Care Providers and Suppliers (Title XVIII) Medicare
93.778 Medical Assistance Program (Medicaid; Title XIX)
Federal Award Number: 1805WA5MAP; 1805WA5ADM; 1805WAIMPL; 1805WAINCT
Applicable Compliance Component: Activities Allowed or Unallowed Allowable Costs/Cost Principles
Known Questioned Cost Amount: \$3,762,678

Background

Medicaid is a jointly funded state and federal partnership providing coverage for about 1.9 million eligible low-income Washington residents who otherwise might go without medical care. Medicaid is Washington’s largest public assistance program and accounts for about one-third of the State’s federal expenditures. The program spent about \$12.7 billion in federal and state funds during fiscal year 2018.

The Health Care Authority (Authority), the state’s Medicaid agency, administers Washington’s managed-care program. Managed care is a prepaid, comprehensive system of medical and health care delivery, including preventive, primary, specialty and ancillary health care services. The program is designed to reduce the cost of providing health benefits, improve the quality of care and deliver health care to clients. The State contracts with health insurance plans, known as managed-care organizations, to cover the costs of Medicaid client claims.

The Authority pays managed-care organizations a uniform, pre-determined per-enrollee monthly premium to cover medical costs for Medicaid eligible clients. In Washington, certain client groups are excluded from managed care, including clients who are eligible to receive Medicare.

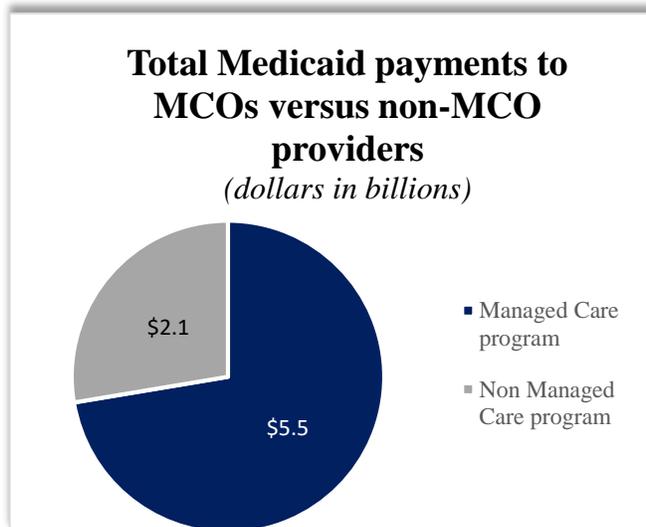
According to Washington’s Medicaid state plan, Medicare recipients should not be enrolled in managed care, and any monthly premium payments made for Medicare recipients are unallowable.

In fiscal year 2018, the state Medicaid program paid about \$5.5 billion in managed-care premiums on behalf of over 1.8 million Medicaid clients.

In the previous audit, we reported the Authority made improper managed care premium payments to Medicaid clients with Medicare insurance coverage. The prior finding number was 2017-039.

Description of Condition

We found the Authority had adequate internal controls to materially ensure it did not make improper payments to managed-care organizations.



We obtained Medicare coverage information from the Authority for all Medicaid-eligible clients. Using computer assisted auditing techniques, we tested to determine if the Authority made monthly managed care premium payments for clients during the same time period when the client's Medicare coverage was effective.

We found 8,753 improper premium payments made on behalf of 5,620 clients who had Medicare coverage during the same month as their monthly, managed care premium payment. The Authority paid \$5,806,346 to the managed-care organizations serving these clients.

Because the questioned costs identified by the audit exceeded \$25,000, federal regulations require the auditor to issue a finding.

Cause of Condition

The Authority had automated processes in place in ProviderOne, the state's Medicaid Management Information System, designed to materially detect clients with Medicare coverage to prevent payments to managed-care organizations for those clients. However, these processes did not prevent or detect all unallowable premium payments.

In its corrective action plan for the prior audit finding, the Authority listed corrective measures it planned to implement during the audit period, including enhancements to ProviderOne to automate the recoupment of managed care premiums for clients who are retroactively enrolled in Medicare. The Authority estimated to complete this action by April 2018. We confirmed this was not completed until June 2018.

The Authority began performing post-payment reviews in March 2016 to detect improper managed-care premiums paid to Medicare recipients during the audit period. The Authority's most recent review began in November 2017. The Authority recovered payments identified during this review in May 2018, however, the review did not address all managed care premium payments that occurred during the audit period.

Effect of Condition and Questioned Costs

Payments that are duplicative or made to an ineligible recipient are unallowable and cannot be claimed for federal reimbursement. As seen in the following table, the federal share of the improper payments totaled \$3,762,678.

Client group	Number of clients	Number of premiums paid	Known questioned costs	Federal share of known questioned costs
Clients with Medicare Part A (hospital) and Part B (physician) coverage	4,900	8,008	\$5,231,962	\$3,393,825
Clients with Medicare Part C (Medicare Advantage Plan) coverage	720	745	\$574,384	\$368,853
Total	5,620	8,753	\$5,806,346	\$3,762,678

We question costs when we find an agency has not complied with grant regulations or when it does not have adequate documentation to support its expenditures.

Recommendations

We recommend the Authority:

- Recoup overpayments made to managed-care organizations identified in the audit
- Consult with the U.S. Department of Health and Human Services to discuss whether the questioned costs identified in the audit should be repaid

Authority's Response

As noted by the State Auditor's Office, the Authority is currently identifying any duplicate per member per month (PMPM) premium payments for clients enrolled in Medicare. The Authority developed an algorithm to identify these duplicate PMPM premium payments in March 2016. Enhancements made to the MMIS/ProviderOne system to automate recoupment of PMPM premiums for clients who are retro-enrolled in Medicare went live on June 8, 2018.

The Authority has run an algorithm identifying all duplicate PMPM premium payments for clients enrolled in Medicare, including the questioned costs, during the gap period from the last algorithm run in November 2017 and the go live system enhancement date of June 8, 2018. These duplicate PMPM premium payments will be recouped by May 31, 2019.

Auditor's Concluding Remarks

We thank the Authority for its cooperation and assistance throughout the audit. We will review the status of the Authority's corrective action during our next audit.

Applicable Laws and Regulations

Title 2 U.S. Code of Federal Regulations Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance) establishes the following applicable requirements:

Section 200.53 Improper Payments states:

- (a) *Improper payment* means any payment that should not have been made or that was made in an incorrect amount (including overpayments and underpayments) under statutory, contractual, administrative, or other legally applicable requirements; and
- (b) *Improper payment* includes any payment to an ineligible party, any payment for an ineligible good or service, any duplicate payment, any payment for a good or service not received (except for such payments where authorized by law), any payment that does not account for credit for applicable discounts, and any payment where insufficient or lack of documentation prevents a reviewer from discerning whether a payment was proper.

Section 200.403 Factors affecting Allowability of costs.

Except where otherwise authorized by statute, costs must meet the following general criteria in order to be allowable under Federal awards.

- (a) Be necessary and reasonable for the performance of the Federal award and be allocable thereto under these principles.
- (b) Conform to any limitations or exclusions set forth in these principles or in the Federal award as to types or amount of cost items.
- (c) Be consistent with policies and procedures that apply uniformly to both federally-financed and other activities of the non-Federal entity.
- (d) Be accorded consistent treatment. A cost may not be assigned to a Federal award as a direct cost if any other cost incurred for the same purpose in like circumstances has been allocated to the Federal award as an indirect cost.
- (e) Be determined in accordance with generally accepted accounting principles (GAAP), except, for state and local governments and Indian tribes only, as otherwise provided for in this part.
- (f) Not be included as a cost or used to meet cost sharing or matching requirements of any other federally-financed program in either the current or a prior period. See also §200.306 Cost sharing or matching paragraph (b).
- (g) Be adequately documented. See also §§200.300 Statutory and national policy requirements through 200.309 Period of performance of this part.

Section 200.410 Collection of unallowable costs.

Payments made for costs determined to be unallowable by either the Federal awarding agency, cognizant agency for indirect costs, or pass-through entity, either as direct or

indirect costs, must be refunded (including interest) to the Federal Government in accordance with instructions from the Federal agency that determined the costs are unallowable unless Federal statute or regulation directs otherwise. See also Subpart D—Post Federal Award Requirements of this part, §§200.300 Statutory and national policy requirements through 200.309 Period of performance.

Section 200.516 Audit findings, states in part:

- (a) *Audit findings reported.* The auditor must report the following as audit findings in a schedule of findings and questioned costs:
 - (3) Known questioned costs that are greater than \$25,000 for a type of compliance requirement for a major program. Known questioned costs are those specifically identified by the auditor. In evaluating the effect of questioned costs on the opinion on compliance, the auditor considers the best estimate of total costs questioned (likely questioned costs), not just the questioned costs specifically identified (known questioned costs). The auditor must also report known questioned costs when likely questioned costs are greater than \$25,000 for a type of compliance requirement for a major program. In reporting questioned costs, the auditor must include information to provide proper perspective for judging the prevalence and consequences of the questioned costs.

Title 42 U.S. Code of Federal Regulations Part 433, State Fiscal Administration, Subpart F – Refunding of Federal Share of Medicaid Overpayments to Providers

Section 433.300 Basis.

This subpart implements -

- (a) Section 1903(d)(2)(A) of the Act, which directs that quarterly Federal payments to the States under title XIX (Medicaid) of the Act are to be reduced or increased to make adjustment for prior overpayments or underpayments that the Secretary determines have been made.
- (b) Section 1903(d)(2)(C) and (D) of the Act, which provides that a State has 1 year from discovery of an overpayment for Medicaid services to recover or attempt to recover the overpayment from the provider before adjustment in the Federal Medicaid payment to the State is made; and that adjustment will be made at the end of the 1-year period, whether or not recovery is made, unless the State is unable to recover from a provider because the overpayment is a debt that has been discharged in bankruptcy or is otherwise uncollectable.

Section 433.316 When discovery of overpayment occurs and its significance, states in part:

- (a) *General rule.* The date on which an overpayment is discovered is the beginning date of the 1-year period allowed for a State to recover or seek to recover an overpayment before a refund of the Federal share of an overpayment must be made to CMS.
- (b) *Requirements for notification.* Unless a State official or fiscal agent of the State chooses to initiate a formal recoupment action against a provider without first giving written notification of its intent, a State Medicaid agency official or other State official must notify the provider in writing of any overpayment it discovers in accordance with State

agency policies and procedures and must take reasonable actions to attempt to recover the overpayment in accordance with State law and procedures.

- (c) *Overpayments resulting from situations other than fraud.* An overpayment resulting from a situation other than fraud is discovered on the earliest of - -
- (1) The date on which any Medicaid agency official or other State official first notifies a provider in writing of an overpayment and specifies a dollar amount that is subject to recovery;
 - (2) The date on which a provider initially acknowledges a specific overpaid amount in writing to the Medicaid agency; or
 - (3) The date on which any State official or fiscal agent of the State initiates a formal action to recoup a specific overpaid amount from a provider without having first notified the provider in writing.

Office of Management and Budget OMB Uniform Guidance, Compliance Supplement for 2017, *Part 4 – Agency Program Requirements, 4.93.778 Medicaid Cluster*, states in part:

General Audit Approach for Medicaid Payments

To be allowable, Medicaid costs for medical services must be (1) covered by the State plan and waivers; (2) reviewed by the State consistent with the State’s documented procedures and system for determining medical necessity of claims; (3) properly coded; and (4) paid at the rate allowed by the State plan. Additionally, Medicaid costs must be net of beneficiary cost-sharing obligations and applicable credits (e.g., insurance, recoveries from other third parties who are responsible for covering the Medicaid costs, and drug rebates), paid to eligible providers, and only provided on behalf of eligible individuals.

Title 42 U.S. Code of Federal Regulations Chapter 7, Social Security, Subchapter XIX – Grants to States For Medical Assistance Programs, § 1396u-2 – Provisions relating to managed care, states in part:

- (a) State Option to Use Managed Care
 - (2) Special Rules
 - (B) Exemption of Medicare beneficiaries.

A state may not require under paragraph (1) the enrollment in a managed care entity of an individual who is a qualified Medicare beneficiary (as defined in section 1396d(p)(1) of this title) or an individual otherwise eligible for benefits under subchapter XVIII.

The Health Care Authority, Apple Health Managed Care Contract, Section 4.3 – “Eligible Client Groups” states in part:

Clients in the following eligibility groups at the time of enrollment are eligible for enrollment under this Contract.

- 4.3.6 Categorically Needy – Blind and Disabled Children and Adults who are not eligible for Medicare.

Medicaid State Plan, Scope of Care and Types of Services, Attachment 3.1 F Part 2, Apple Health Managed Care, E. Populations and Geographic Area, states in part:

2. Voluntary Only or Excluded Populations. Under this managed care authority, some populations cannot be subject to mandatory enrollment in an MCO, PCCM, or PCCM entity (per 42 CFR 438.50(d)).

Please indicate if any of the following populations are excluded from the program, or have only voluntary enrollment (even if they are part of an eligibility group listed above in E.1. as having mandatory enrollment):

Population	Citation (Regulation [42 CFR] or	Voluntary	Excluded	Geographic Area	Notes
Medicare Savings Program – Qualified Medicare Beneficiaries, Qualified Disabled Working Individuals, Specified Low Income Medicare Beneficiaries, and/or Qualifying Individuals	1902(a)(10)(E), 1905(p), 1905(s) of the SSA		X		Not currently eligible for Medicaid Managed Care

2018-050 The Department of Social and Health Services, Aging and Long-Term Support Administration, made improper Medicaid payments to individual providers when clients were hospitalized or admitted to long-term care facilities.

Federal Awarding Agency: U.S. Department of Health and Human Services
Pass-Through Entity: None
CFDA Number and Title: 93.775 State Medicaid Fraud Control Units
93.777 State Survey and Certification of Health Care Providers and Suppliers (Title XVIII) Medicare
93.778 Medical Assistance Program (Medicaid; Title XIX)
Federal Award Number: 1805WA5MAP; 1805WA5ADM; 1805WAIMPL; 1805WAINCT
Applicable Compliance Component: Activities Allowed/Unallowed Allowable Costs/Cost Principles
Known Questioned Cost Amount: \$325,468
(\$259,385 - Personal care and transportation services)
(\$66,083 - Associated costs)

Background

Medicaid is a jointly funded state and federal partnership providing coverage for about 1.9 million eligible low-income Washington residents who otherwise might go without medical care. Medicaid is Washington’s largest public assistance program and accounts for about one-third of the State’s federal expenditures. The program spent about \$12.7 billion in federal and state funds during fiscal year 2018.

The Aging and Long-Term Support Administration within the Department of Social and Health Services (Department) offers personal care services to support Medicaid clients in community settings through the Community First Choice program. The Department uses an assessment to evaluate a client’s support needs and to calculate the number of personal care hours the client needs to successfully live in the community. Individual providers contract with the Department to provide personal care services to clients.

In fiscal year 2018, the state Medicaid program paid about \$607 million to Aging and Long-Term Support Administration’s contracted Community First Choice individual providers who provided personal care and transportation services.

Individual providers are paid an hourly rate for providing personal care and a mileage rate for providing transportation services to their clients. Individual providers use the Department’s Individual ProviderOne system to invoice the Department for their hourly service and mileage claims. At times, a Medicaid client may be hospitalized or temporarily admitted to a long-term care facility, which the Health Care Authority (Authority) is responsible to pay for. In those cases, individual providers are not

allowed to bill for services because Medicaid pays the hospital or care facility for the client’s care while admitted to the facility.

In fiscal years 2016 and 2017, we found the Department made improper Medicaid payments to individual providers when clients were hospitalized or in a long-term care facility. In 2016, we issued finding number 2016-048. In fiscal year 2017, we did not issue a finding because we could not determine whether the duplicate expenditures were individual provider billing errors or hospital or long-term care facility billing errors.

Description of Condition

We found the Department had established adequate internal controls to ensure it was in material compliance with allowable costs over payments to individual providers.

However, we found the Department made unallowable payments to some individual providers who claimed payment for personal care and transportation services while their client was either hospitalized or admitted to a long-term care facility.

Because the questioned costs identified by the audit exceeded \$25,000, federal regulations requires the auditor to issue a finding.

Cause of Condition

The Department did not have a process or a system edit in place to prevent unallowable claims or to detect these payments after the unallowable claims were made.

Effect of Condition and Questioned Costs

In the current audit we identified at least \$582,243 was improperly paid to providers.

We provided the results of our tests to the Department in October 2018, but it did not verify whether the unallowable payments were made to the individual provider or the hospital/long-term care facility. Our calculation of the unallowable payments was based on payments to the individual providers. If the Department determines any of the unallowable payments were made to a hospital or long-term care facility, the amount of the question costs would be higher. In those instances, the Authority would be responsible for collecting provider overpayments and refunding improper Medicaid payments to the grantor.



In the prior two audits, we reported the unallowable payments to individual providers increased. In addition, the Department has not followed up on exceptions identified in the prior year audits.

We are questioning \$259,386, which is the federal portion of the unallowable payments for personal care and transportation services.

When unallowable payments are identified, federal regulations suggest auditors consider if associated costs, such as benefits, were also paid. The Department pays payroll tax and health care, training and retirement fringe benefits on behalf of Community First Choice providers that are considered associated costs.

We are also questioning at least \$66,083, which is the federal portion of the unallowable payments related to associated costs. The Department contracts with a vendor that manages IPOne. The system is currently unable to make overpayment adjustments and until the issue is resolved, the Department will not know the exact amount of associated costs to refund the grantor. In addition, the system has been unable to correctly calculate State Unemployment Tax Act (SUTA) taxes since it began processing payroll on April 1, 2016.

Description	Total known questioned costs	Known questioned costs – federal portion only
Personal care and transportation claims	\$464,238	\$259,385
Associated costs	\$118,005	\$66,083
Total	\$582,243	\$325,468

The statistical sample used for testing in parts of the fiscal year 2018 Medicaid audit was used to test compliance with other activities allowed requirements. Because some unallowable payments we examined violated multiple areas of activities allowed some of the questioned costs reported here might also be reported in finding numbers 2018-051, 2018-055, 2018-056, 2018-059, and 2018-060.

We question costs when we find an agency has not complied with grant regulations or when it does not have adequate documentation to support its expenditures.

Recommendations

We recommend the Department:

- Follow-up on the improper Medicaid claims identified by the audit. In some cases, the Department may need to consult with the Authority to determine the individual provider or facility was improperly paid
- Identify all associated costs related to the unallowable payments for personal care services
- Consult with the U.S. Department of Health and Human Services to discuss whether the questioned costs identified in the audit should be repaid

Department's Response

The Department partially concurs with this finding.

The Department concurs that unallowable payments were made, but it is not known whether payments were incorrectly claimed by the individual provider rather than the hospital or nursing facility. The SAO stated in fiscal year 2017 that it "did not issue a finding because we could not determine whether the duplicate expenditures were individual provider billing errors or hospital or long-term care facility billing errors." For this year's 2018 audit, the SAO used the same audit methodology and issued a finding without explaining a rationale as to how they were able to determine who made the billing error or why these errors were attributed to the Department.

To address the unallowable payments the Department created a report in October of 2018 to identify payments made to all provider types for in-home personal care and mileage services while the client was in the hospital or in a long-term care facility. In November of 2018, a new Washington Management System position was created and an employee was hired to complete the payment analysis and coordinate remediation with field contacts. Reviewing, tracking and processing of these findings began late January 2019.

The Department will analyze the payments in question and consult with the Health Care Authority to determine which entity is responsible for the unallowable payments. If any unallowable payments are determined to be the Department's responsibility, the Department will begin the process of issuing overpayments to its identified providers. Individual provider overpayment functionality in the IPhone payment system is currently in testing and targeted for implementation to the field May 2019. Once overpayments are completed, if necessary, the Department will consult with the Department of Health and Human Services to discuss remaining questioned costs.

Auditor's Concluding Remarks

We used the same methodology in the 2017 and 2018 audits to identify instances when payments to individual providers were made when clients were hospitalized or in long-term care facilities. For this audit, we provided the duplicate payment data to the Department for its review early on in the audit and provided ample time for it to review the results. We received confirmation from the Department that it concurred with the exceptions.

Because the questioned costs identified in the audit were at least \$25,000, federal regulations require us to issue an audit finding.

During the audit period, the Department had not implemented an internal control to detect and prevent duplicate payments. We reaffirm our finding and will review the status of the Department's corrective action during our next audit.

Applicable Laws and Regulations

Title 2 U.S. Code of Federal Regulations Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance) establishes the following applicable requirements:

Section 200.53 Improper Payments states in part:

- (a) *Improper payment* means any payment that should not have been made or that was made in an incorrect amount (including overpayments and underpayments) under statutory, contractual, administrative, or other legally applicable requirements; and
- (b) *Improper payment* includes any payment to an ineligible party, any payment for an ineligible good or service, any duplicate payment, any payment for a good or service not received (except for such payments where authorized by law), any payment that does not account for credit for applicable discounts, and any payment where insufficient or lack of documentation prevents a reviewer from discerning whether a payment was proper.

Section 200.403 Factors affecting Allowability of costs.

Except where otherwise authorized by statute, costs must meet the following general criteria in order to be allowable under Federal awards.

- (a) Be necessary and reasonable for the performance of the Federal award and be allocable thereto under these principles.
- (b) Conform to any limitations or exclusions set forth in these principles or in the Federal award as to types or amount of cost items.
- (c) Be consistent with policies and procedures that apply uniformly to both federally-financed and other activities of the non-Federal entity.
- (d) Be accorded consistent treatment. A cost may not be assigned to a Federal award as a direct cost if any other cost incurred for the same purpose in like circumstances has been allocated to the Federal award as an indirect cost.
- (e) Be determined in accordance with generally accepted accounting principles (GAAP), except, for state and local governments and Indian tribes only, as otherwise provided for in this part.
- (f) Not be included as a cost or used to meet cost sharing or matching requirements of any other federally-financed program in either the current or a prior period. See also §200.306 Cost sharing or matching paragraph (b).
- (g) Be adequately documented. See also §§200.300 Statutory and national policy requirements through 200.309 Period of performance of this part.

Section 200.410 Collection of unallowable costs.

Payments made for costs determined to be unallowable by either the Federal awarding agency, cognizant agency for indirect costs, or pass-through entity, either as direct or indirect costs, must be refunded (including interest) to the Federal Government in accordance with instructions from the Federal agency that determined the costs are unallowable unless Federal statute or regulation directs otherwise. See also Subpart D—Post Federal Award Requirements of this part, §§200.300 Statutory and national policy requirements through 200.309 Period of performance.

Section 200.516 Audit findings, states in part:

- (a) *Audit findings reported.* The auditor must report the following as audit findings in a schedule of findings and questioned costs:
 - (3) Known questioned costs that are greater than \$25,000 for a type of compliance requirement for a major program. Known questioned costs are those specifically identified by the auditor. In evaluating the effect of questioned costs on the opinion on compliance, the auditor considers the best estimate of total costs questioned (likely questioned costs), not just the questioned costs specifically identified (known questioned costs). The auditor must also report known questioned costs when likely questioned costs are greater than \$25,000 for a type of compliance requirement for a major program. In reporting questioned costs, the auditor must include information to provide proper perspective for judging the prevalence and consequences of the questioned costs.

Title 42 U.S. Code of Federal Regulations Part 433, State Fiscal Administration, Subpart F – Refunding of Federal Share of Medicaid Overpayments to Providers states in part:

Section 433.300 Basis.

This subpart implements -

- (a) Section 1903(d)(2)(A) of the Act, which directs that quarterly Federal payments to the States under title XIX (Medicaid) of the Act are to be reduced or increased to make adjustment for prior overpayments or underpayments that the Secretary determines have been made.
- (b) Section 1903(d)(2)(C) and (D) of the Act, which provides that a State has 1 year from discovery of an overpayment for Medicaid services to recover or attempt to recover the overpayment from the provider before adjustment in the Federal Medicaid payment to the State is made; and that adjustment will be made at the end of the 1-year period, whether or not recovery is made, unless the State is unable to recover from a provider because the overpayment is a debt that has been discharged in bankruptcy or is otherwise uncollectable.

Section 433.316 When discovery of overpayment occurs and its significance.

- (a) *General rule.* The date on which an overpayment is discovered is the beginning date of the 1-year period allowed for a State to recover or seek to recover an overpayment before a refund of the Federal share of an overpayment must be made to CMS.
- (b) *Requirements for notification.* Unless a State official or fiscal agent of the State chooses to initiate a formal recoupment action against a provider without first giving written notification of its intent, a State Medicaid agency official or other State official must notify the provider in writing of any overpayment it discovers in accordance with State agency policies and procedures and must take reasonable actions to attempt to recover the overpayment in accordance with State law and procedures.
- (c) *Overpayments resulting from situations other than fraud.* An overpayment resulting from a situation other than fraud is discovered on the earliest of - -

- (1) The date on which any Medicaid agency official or other State official first notifies a provider in writing of an overpayment and specifies a dollar amount that is subject to recovery;
 - (2) The date on which a provider initially acknowledges a specific overpaid amount in writing to the medicaid agency; or
 - (3) The date on which any State official or fiscal agent of the State initiates a formal action to recoup a specific overpaid amount from a provider without having first notified the provider in writing.
- (d) *Overpayments resulting from fraud.*
- (1) An overpayment that results from fraud is discovered on the date of the final written notice (as defined in § 433.304 of this subchapter) of the State's overpayment determination.
 - (2) When the State is unable to recover a debt which represents an overpayment (or any portion thereof) resulting from fraud within 1 year of discovery because no final determination of the amount of the overpayment has been made under an administrative or judicial process (as applicable), including as a result of a judgment being under appeal, no adjustment shall be made in the Federal payment to such State on account of such overpayment (or any portion thereof) until 30 days after the date on which a final judgment (including, if applicable, a final determination on an appeal) is made.
 - (3) The Medicaid agency may treat an overpayment made to a Medicaid provider as resulting from fraud under subsection (d) of this section only if it has referred a provider's case to the Medicaid fraud control unit, or appropriate law enforcement agency in States with no certified Medicaid fraud control unit, as required by § 455.15, § 455.21, or § 455.23 of this chapter, and the Medicaid fraud control unit or appropriate law enforcement agency has provided the Medicaid agency with written notification of acceptance of the case; or if the Medicaid fraud control unit or appropriate law enforcement agency has filed a civil or criminal action against a provider and has notified the State Medicaid agency.
- (e) *Overpayments identified through Federal reviews.* If a Federal review at any time indicates that a State has failed to identify an overpayment or a State has identified an overpayment but has failed to either send written notice of the overpayment to the provider that specified a dollar amount subject to recovery or initiate a formal recoupment from the provider without having first notified the provider in writing, CMS will consider the overpayment as discovered on the date that the Federal official first notifies the State in writing of the overpayment and specifies a dollar amount subject to recovery.
- (f) *Effect of changes in overpayment amount.* Any adjustment in the amount of an overpayment during the 1-year period following discovery (made in accordance with the approved State plan, Federal law and regulations governing Medicaid, and the appeals resolution process specified in State administrative policies and procedures) has the following effect on the 1-year recovery period:
- (1) A downward adjustment in the amount of an overpayment subject to recovery that occurs after discovery does not change the original 1-year recovery period for the outstanding balance.

- (2) An upward adjustment in the amount of an overpayment subject to recovery that occurs during the 1-year period following discovery does not change the 1-year recovery period for the original overpayment amount. A new 1-year period begins for the incremental amount only, beginning with the date of the State's written notification to the provider regarding the upward adjustment.
- (g) *Effect of partial collection by State.* A partial collection of an overpayment amount by the State from a provider during the 1-year period following discovery does not change the 1-year recovery period for the balance of the original overpayment amount due to CMS.
- (h) *Effect of administrative or judicial appeals.* Any appeal rights extended to a provider do not extend the date of discovery.

Office of Management and Budget OMB Uniform Guidance, Compliance Supplement for 2017, *Part 4 – Agency Program Requirements, 4.93.778 Medicaid Cluster*, states in part:

General Audit Approach for Medicaid Payments

To be allowable, Medicaid costs for medical services must be (1) covered by the State plan and waivers; (2) reviewed by the State consistent with the State's documented procedures and system for determining medical necessity of claims; (3) properly coded; and (4) paid at the rate allowed by the State plan. Additionally, Medicaid costs must be net of beneficiary cost-sharing obligations and applicable credits (e.g., insurance, recoveries from other third parties who are responsible for covering the Medicaid costs, and drug rebates), paid to eligible providers, and only provided on behalf of eligible individuals.

2018-051 The Department of Social and Health Services, Developmental Disabilities Administration, made improper Medicaid payments to individual providers when clients were hospitalized or admitted to long-term care facilities.

Federal Awarding Agency: U.S. Department of Health and Human Services
Pass-Through Entity: None
CFDA Number and Title: 93.775 State Medicaid Fraud Control Units
93.777 State Survey and Certification of Health Care Providers and Suppliers (Title XVIII) Medicare
93.778 Medical Assistance Program (Medicaid; Title XIX)
Federal Award Number: 1805WA5MAP; 1805WA5ADM; 1805WAIMPL; 1805WAINCT
Applicable Compliance Component: Activities Allowed/Unallowed Allowable Costs/Cost Principles
Known Questioned Cost Amount: \$34,510
(\$27,473 – Personal care and transportation services)
(\$7,037 – Associated costs)

Background

Medicaid is a jointly funded state and federal partnership providing coverage for about 1.9 million eligible low-income Washington residents who otherwise might go without medical care. Medicaid is Washington’s largest public assistance program and accounts for about one-third of the State’s federal expenditures. The program spent about \$12.7 billion in federal and state funds during fiscal year 2018.

The Developmental Disabilities Administration within the Department of Social and Health Services (Department) offers personal care services to support Medicaid clients in community settings through the Community First Choice program. The Department uses an assessment to evaluate a client’s support needs and to calculate the number of personal care hours the client needs to successfully live in the community. Individual providers contract with the Department to provide personal care services to clients.

In fiscal year 2018, the state Medicaid program paid about \$272 million to Developmental Disabilities Administration’s contracted Community First Choice individual providers who provided personal care and transportation services.

Individual providers are paid an hourly rate for providing personal care and a mileage rate for providing transportation services to their clients. Individual providers use the Department’s Individual ProviderOne (IPOne) system to invoice the Department for their hourly service and mileage claims. At times, a Medicaid client may be hospitalized or temporarily admitted to a long-term care facility. Individual providers are not allowed to bill for services provided to the client during the period of their

admission because Medicaid funding is used by the Health Care Authority (Authority) to pay the hospital or care facility for the client's care during this period of time.

This condition was not reported in the prior audit.

Description of Condition

We found the Department established adequate internal controls to ensure payments to individual providers were materially allowable.

However, we found the Department made unallowable payments to some individual providers who claimed payment for personal care and transportation services when a Medicaid client was either hospitalized or admitted to a long-term care facility.

Because the questioned costs identified by the audit exceeded \$25,000, federal regulations require the auditor to issue a finding.

Cause of Condition

The Department did not have a process or system edit in place to prevent the unallowable claims or to detect the payments after the unallowable claims were made.

Effect of Condition and Questioned Costs

We compared claims made by individual providers with claims made by hospitals and long-term care facilities for inpatient services to determine if duplicate claims were paid on the same date of service. We provided the results of our test to the Department, and it reviewed the results. We worked with the Authority on claims the Department believed could have been attributed to inaccurate billing by a hospital or long-term care facility.

After the reviews, the Department confirmed that at least \$49,121 was improperly paid to providers for personal care and transportation services. No improper claims were made by hospitals or long-term care facilities.

We are questioning \$27,473, which is the federal portion of the unallowable payments for personal care and transportation services.

When unallowable payments are identified, federal regulations suggest auditors consider if associated costs, such as benefits, were also paid. The Department pays payroll tax and health care, training and retirement fringe benefits on behalf of Community First Choice providers that are considered associated costs.

We are also questioning at least \$7,037, which is the federal portion of the unallowable payments related to associated costs. The Department contracts with a vendor that manages IPOne. The system is currently unable to make overpayment adjustments and until the issue is resolved, the Department will not know the exact amount of associated costs to refund the grantor. In addition, the system has

been unable to correctly calculate State Unemployment Tax Act (SUTA) taxes since it began processing payroll on April 1, 2016.

Description	Total know questioned costs	Known questioned costs – federal portion only
Personal care and transportation claims	\$49,121	\$27,473
Associated costs	\$12,567	\$7,037
Totals	\$61,688	\$34,510

The statistical sample used for testing in parts of the fiscal year 2018 Medicaid audit was used to test compliance with other activities allowed requirements. Because some unallowable payments we examined violated multiple areas of activities allowed some of the questioned costs reported here might also be reported in finding numbers 2018-050, 2018-055, 2018-056, 2018-059, and 2018-060.

We question costs when we find an agency has not complied with grant regulations or when it does not have adequate documentation to support its expenditures.

Recommendations

We recommend the Department:

- Identify all associated costs related to the unallowable payments for personal care services
- Consult with the U.S. Department of Health and Human Services to discuss whether the questioned costs identified in the audit and associated costs should be repaid.

Department’s Response

The Department concurs with the finding.

To address the unallowable payments the Department will enhance monitoring procedures for identifying unallowable payments. The Department will work with the federal grantor to determine if any costs charged to Medicaid fund must be reimbursed.

The Department would also like to note, that SAO stated in fiscal year 2017 that it “did not issue a finding because we could not determine whether the duplicate expenditures were individual provider billing errors or hospital or long-term care facility billing errors.” For this year’s 2018 audit, the SAO used the same audit methodology and issued a finding without explaining a rationale as to how they were able to determine who made the billing error or why these errors were attributed to the Department.

Auditor's Concluding Remarks

During the fiscal year 2017 audit, we issued an exit item to the Developmental Disabilities Administration related to this audit area because known questioned costs were not greater than \$25,000.

We used the same methodology in the 2017 and 2018 audits to identify instances when payments to individual providers were made when clients were hospitalized or in long-term care facilities. For this audit, we provided the data to the Department and asked it to review the duplicate payments. For those claims that the Department could not determine if a facility inaccurately billed or if the individual provider inaccurately billed, we worked with the Department and the Authority to follow up on those claims. Our work with the Authority found supporting admission and discharge documentation from the hospitals that indicated the clients were hospitalized during the time the individual providers claimed payment.

Because the questioned costs identified in the audit were at least \$25,000, federal regulations require us to issue an audit finding.

We will review the status of the Department's corrective action during our next audit.

Applicable Laws and Regulations

Title 2 U.S. Code of Federal Regulations Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance) establishes the following applicable requirements:

Section 200.53 Improper Payments states in part:

- (a) *Improper payment* means any payment that should not have been made or that was made in an incorrect amount (including overpayments and underpayments) under statutory, contractual, administrative, or other legally applicable requirements; and
- (b) *Improper payment* includes any payment to an ineligible party, any payment for an ineligible good or service, any duplicate payment, any payment for a good or service not received (except for such payments where authorized by law), any payment that does not account for credit for applicable discounts, and any payment where insufficient or lack of documentation prevents a reviewer from discerning whether a payment was proper.

Section 200.403 Factors affecting Allowability of costs.

Except where otherwise authorized by statute, costs must meet the following general criteria in order to be allowable under Federal awards.

- (a) Be necessary and reasonable for the performance of the Federal award and be allocable thereto under these principles.
- (b) Conform to any limitations or exclusions set forth in these principles or in the Federal award as to types or amount of cost items.
- (c) Be consistent with policies and procedures that apply uniformly to both federally-financed and other activities of the non-Federal entity.

- (d) Be accorded consistent treatment. A cost may not be assigned to a Federal award as a direct cost if any other cost incurred for the same purpose in like circumstances has been allocated to the Federal award as an indirect cost.
- (e) Be determined in accordance with generally accepted accounting principles (GAAP), except, for state and local governments and Indian tribes only, as otherwise provided for in this part.
- (f) Not be included as a cost or used to meet cost sharing or matching requirements of any other federally-financed program in either the current or a prior period. See also §200.306 Cost sharing or matching paragraph (b).
- (g) Be adequately documented. See also §§200.300 Statutory and national policy requirements through 200.309 Period of performance of this part.

Section 200.410 Collection of unallowable costs.

Payments made for costs determined to be unallowable by either the Federal awarding agency, cognizant agency for indirect costs, or pass-through entity, either as direct or indirect costs, must be refunded (including interest) to the Federal Government in accordance with instructions from the Federal agency that determined the costs are unallowable unless Federal statute or regulation directs otherwise. See also Subpart D— Post Federal Award Requirements of this part, §§200.300 Statutory and national policy requirements through 200.309 Period of performance.

Section 200.516 Audit findings, states in part:

- (a) *Audit findings reported.* The auditor must report the following as audit findings in a schedule of findings and questioned costs:
 - (3) Known questioned costs that are greater than \$25,000 for a type of compliance requirement for a major program. Known questioned costs are those specifically identified by the auditor. In evaluating the effect of questioned costs on the opinion on compliance, the auditor considers the best estimate of total costs questioned (likely questioned costs), not just the questioned costs specifically identified (known questioned costs). The auditor must also report known questioned costs when likely questioned costs are greater than \$25,000 for a type of compliance requirement for a major program. In reporting questioned costs, the auditor must include information to provide proper perspective for judging the prevalence and consequences of the questioned costs.

Title 42 U.S. Code of Federal Regulations Part 433, State Fiscal Administration, Subpart F – Refunding of Federal Share of Medicaid Overpayments to Providers states in part:

Section 433.300 Basis.

This subpart implements -

- (a) Section 1903(d)(2)(A) of the Act, which directs that quarterly Federal payments to the States under title XIX (Medicaid) of the Act are to be reduced or increased to make adjustment for prior overpayments or underpayments that the Secretary determines have been made.
- (b) Section 1903(d)(2)(C) and (D) of the Act, which provides that a State has 1 year from discovery of an overpayment for Medicaid services to recover or attempt to

recover the overpayment from the provider before adjustment in the Federal Medicaid payment to the State is made; and that adjustment will be made at the end of the 1-year period, whether or not recovery is made, unless the State is unable to recover from a provider because the overpayment is a debt that has been discharged in bankruptcy or is otherwise uncollectable.

Section 433.316 When discovery of overpayment occurs and its significance.

- (a) *General rule.* The date on which an overpayment is discovered is the beginning date of the 1-year period allowed for a State to recover or seek to recover an overpayment before a refund of the Federal share of an overpayment must be made to CMS.
- (b) *Requirements for notification.* Unless a State official or fiscal agent of the State chooses to initiate a formal recoupment action against a provider without first giving written notification of its intent, a State Medicaid agency official or other State official must notify the provider in writing of any overpayment it discovers in accordance with State agency policies and procedures and must take reasonable actions to attempt to recover the overpayment in accordance with State law and procedures.
- (c) *Overpayments resulting from situations other than fraud.* An overpayment resulting from a situation other than fraud is discovered on the earliest of - -
 - (1) The date on which any Medicaid agency official or other State official first notifies a provider in writing of an overpayment and specifies a dollar amount that is subject to recovery;
 - (2) The date on which a provider initially acknowledges a specific overpaid amount in writing to the medicaid agency; or
 - (3) The date on which any State official or fiscal agent of the State initiates a formal action to recoup a specific overpaid amount from a provider without having first notified the provider in writing.
- (d) *Overpayments resulting from fraud.*
 - (1) An overpayment that results from fraud is discovered on the date of the final written notice (as defined in § 433.304 of this subchapter) of the State's overpayment determination.
 - (2) When the State is unable to recover a debt which represents an overpayment (or any portion thereof) resulting from fraud within 1 year of discovery because no final determination of the amount of the overpayment has been made under an administrative or judicial process (as applicable), including as a result of a judgment being under appeal, no adjustment shall be made in the Federal payment to such State on account of such overpayment (or any portion thereof) until 30 days after the date on which a final judgment (including, if applicable, a final determination on an appeal) is made.
 - (3) The Medicaid agency may treat an overpayment made to a Medicaid provider as resulting from fraud under subsection (d) of this section only if it has referred a provider's case to the Medicaid fraud control unit, or appropriate law enforcement agency in States with no certified Medicaid fraud control unit, as required by § 455.15, § 455.21, or § 455.23 of this chapter, and the Medicaid fraud control unit or appropriate law enforcement agency has provided the Medicaid agency with written notification of acceptance of the case; or if the Medicaid fraud control unit or

appropriate law enforcement agency has filed a civil or criminal action against a provider and has notified the State Medicaid agency.

- (e) *Overpayments identified through Federal reviews.* If a Federal review at any time indicates that a State has failed to identify an overpayment or a State has identified an overpayment but has failed to either send written notice of the overpayment to the provider that specified a dollar amount subject to recovery or initiate a formal recoupment from the provider without having first notified the provider in writing, CMS will consider the overpayment as discovered on the date that the Federal official first notifies the State in writing of the overpayment and specifies a dollar amount subject to recovery.
- (f) *Effect of changes in overpayment amount.* Any adjustment in the amount of an overpayment during the 1-year period following discovery (made in accordance with the approved State plan, Federal law and regulations governing Medicaid, and the appeals resolution process specified in State administrative policies and procedures) has the following effect on the 1-year recovery period:
 - (1) A downward adjustment in the amount of an overpayment subject to recovery that occurs after discovery does not change the original 1-year recovery period for the outstanding balance.
 - (2) An upward adjustment in the amount of an overpayment subject to recovery that occurs during the 1-year period following discovery does not change the 1-year recovery period for the original overpayment amount. A new 1-year period begins for the incremental amount only, beginning with the date of the State's written notification to the provider regarding the upward adjustment.
- (g) *Effect of partial collection by State.* A partial collection of an overpayment amount by the State from a provider during the 1-year period following discovery does not change the 1-year recovery period for the balance of the original overpayment amount due to CMS.
- (h) *Effect of administrative or judicial appeals.* Any appeal rights extended to a provider do not extend the date of discovery.

Office of Management and Budget OMB Uniform Guidance, Compliance Supplement for 2017, *Part 4 – Agency Program Requirements, 4.93.778 Medicaid Cluster*, states in part:

General Audit Approach for Medicaid Payments

To be allowable, Medicaid costs for medical services must be (1) covered by the State plan and waivers; (2) reviewed by the State consistent with the State's documented procedures and system for determining medical necessity of claims; (3) properly coded; and (4) paid at the rate allowed by the State plan. Additionally, Medicaid costs must be net of beneficiary cost-sharing obligations and applicable credits (e.g., insurance, recoveries from other third parties who are responsible for covering the Medicaid costs, and drug rebates), paid to eligible providers, and only provided on behalf of eligible individuals.

2018-052 The Department of Social and Health Services, Aging and Long-Term Support Administration, did not have adequate internal controls and did not comply with survey requirements for Medicaid intermediate care facilities.

Federal Awarding Agency: U.S. Department of Health and Human Services
Pass-Through Entity: None
CFDA Number and Title: 93.775 State Medicaid Fraud Control Units
93.777 State Survey and Certification of Health Care Providers and Suppliers (Title XVIII) Medicare
93.778 Medical Assistance Program (Medicaid; Title XIX)
Federal Award Number: 1805WA5MAP; 1805WA5ADM; 1805WAIMPL; 1805WAINCT
Applicable Compliance Component: Special Tests and Provisions – Provider Health and Safety Standards
Known Questioned Cost Amount: None

Background

Medicaid is a jointly funded state and federal partnership providing coverage for about 1.9 million eligible low-income Washington residents who otherwise might go without medical care. Medicaid is Washington’s largest public assistance program and accounts for about one-third of the State’s federal expenditures. The program spent about \$13.2 billion in federal and state funds during fiscal year 2018.

Residential Care Services, under the Department of Social and Health Services (Department), Aging and Long-Term Support Administration, is the State’s Intermediate Care Facilities for Individuals with Intellectual Disabilities (ICF/IID) survey agency. An ICF/IID is an institution with the primary purpose of providing health or rehabilitation services to people with intellectual disabilities or related conditions that receive care and services under Medicaid. There are 11 ICF/IID facilities that are Medicare and/or Medicaid certified in Washington.

The Department is required to perform an annual certification survey of each ICF/IID. The certification survey is a resident-centered inspection that gathers information about the quality of service provided in a facility to determine compliance with the participation requirements. The survey focuses on the facility’s administration and patient services, as well as the outcome of the facility’s implementation of ICF/IID active treatment services. The survey also assesses compliance with federal health, safety and quality standards designed to ensure patients receive safe and quality care services.

The State must complete a standard survey for each ICF/IID facility within 15.9 months after the previous survey, and the statewide average for all ICF/IID facilities must not exceed 12.9 months for all ICF/IID facilities, as required by Centers for Medicare and Medicaid Services (CMS). If a survey uncovers deficiencies, the Department must mail a Statement of Deficiency to the facility within 10

working days of the survey date. The facility must submit a Plan of Correction that the Department determines is acceptable within 60 calendar days of receipt or risk forfeiting its Medicaid certification.

In fiscal year 2018, the state Medicaid program spent about \$17.4 million to survey and certify healthcare providers – \$8.9 million was spent to certify ICF/IID facilities.

In prior audits, we reported the Department did not have adequate internal controls to ensure timely conducting of surveys and following up on deficiencies. The prior finding numbers were 2017-042, 2016-037, 2015-045, and 2014-046.

Description of Condition

The Department's Aging and Long-Term Support Administration did not have adequate internal controls over and did not comply with survey requirements for Medicaid intermediate care facilities.

We found the Department did not adequately monitor ICF/IID facilities to ensure that all recertification surveys were completed promptly.

We consider this internal control deficiency to be a material weakness.

Cause of Condition

The facility survey that occurred after the required due date was the result of outstanding noncompliance with Conditions of Participation by the facility. During the prior certification survey, the Department cited the facility for two condition-level deficiencies and the Department had imposed a Denial of Payment for New Admissions as an enforcement action. This matter was not considered to be resolved until a follow-up survey conducted in March 2018 determined the facility was complying with conditions for participation. The next annual recertification survey for this facility was due in April 2018. However, during this time the facility had been subject to multiple surveys and the Department did not have staff available to schedule the certification survey because of other scheduling conflicts.

Effect of Condition

We examined all 11 certification surveys completed during the audit period and found one instance (9 percent) when the Department failed to complete the certification survey within 15.9 months of the previous certification survey. The Department did not materially comply with federal requirements for completing recertification surveys in a timely manner.

When surveys are not conducted timely, the state is paying the facilities for services provided to Medicaid clients without assurance they are in compliance with federal and state health standards and regulations.

Recommendation

We recommend the Department establish adequate internal controls to ensure it complies with facility survey timeliness requirements.

Department's Response

The Department partially agrees with the finding.

The Department has an established internal control that tracks when recertification surveys were completed and when recertification surveys are due. The ineffectiveness of the internal control was not what caused the recertification to be completed late. The Department concurs the recertification survey was not completed within the required 15.99 timelines. This facility, (Facility A) was imposed with a Denial of Payment for new admissions remedy from a prior recertification survey (12/7/2016) resulting from non-compliance with Conditions of Participation (COP). After the Department received this facility's credible allegation of compliance letter on 1/15/2018, the Department conducted two re-survey visits and subsequently put them back in compliance on 3/28/2018. Their next recertification survey, due no later than 4/4/2018, was completed on 5/23/2018.

The Department made an executive decision to prioritize a recertification survey at another facility (Facility B) that had been out of substantial compliance with a COP placing clients' safety and welfare at risk, versus completing the recertification for Facility A, which was recently put back in compliance on 3/28/18. The recertification survey for Facility B completed on 4/19/2018, lead to the facility being out of compliance, resulting in a recommendation for termination.

In addition to continuous monitoring of the survey tracking tool, the Department will request assistance from certified ICF/IID surveyors from other units within Residential Care Services and the Centers for Medicare and Medicaid Services, if necessary, to ensure compliance with survey intervals.

Auditor's Concluding Remarks

We thank the Department for its cooperation and assistance throughout the audit. We will review the status of the Department's corrective action during our next audit.

Applicable Laws and Regulations

Title 2 U.S. Code of Federal Regulations Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance) establishes the following applicable requirements:

Section 200.303 Internal controls, states in part:

The non-Federal entity must:

- (a) Establish and maintain effective internal control over the Federal award that provides reasonable assurance that the non-Federal entity is managing the Federal award in compliance with Federal statutes, regulations, and the terms and conditions of the Federal award. These internal controls should be in compliance with guidance in "Standards for Internal Control in the Federal Government" issued by the Comptroller

General of the United States or the “Internal Control Integrated Framework”, issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).

- (b) Comply with Federal statutes, regulations, and the terms and conditions of the Federal awards.
- (d) Take prompt action when instances of noncompliance are identified including noncompliance identified in audit findings.

Section 200.516 Audit findings, states in part:

- (a) *Audit findings reported.* The auditor must report the following as audit findings in a schedule of findings and questioned costs:
 - (1) Significant deficiencies and material weaknesses in internal control over major programs and significant instances of abuse relating to major programs. The auditor’s determination of whether a deficiency in internal control is a significant deficiency or material weakness for the purpose of reporting an audit finding is in relation to a type of compliance requirement for a major program identified in the Compliance Supplement.
 - (2) Material noncompliance with the provisions of Federal statutes, regulations, or the terms and conditions of Federal awards related to a major program. The auditor’s determination of whether a noncompliance with the provisions of Federal statutes, regulations, or the terms and conditions of Federal awards is material for the purpose of reporting an audit finding is in relation to a type of compliance requirement for a major program identified in the compliance supplement.

The American Institute of Certified Public Accountants defines significant deficiencies and material weaknesses in internal controls over compliance in its *Codification of Statements on Auditing Standards*, section 935, Compliance Audits, as follows:

.11 For purposes of adapting GAAS to a compliance audit, the following terms have the meanings attributed as follows: ...

Deficiency in internal control over compliance. A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance on a timely basis. A deficiency in design exists when (a) a control necessary to meet the control objective is missing, or (b) an existing control is not properly designed so that, even if the control operates as designed, the control objective would not be met. A deficiency in operation exists when a properly designed control does not operate as designed or the person performing the control does not possess the necessary authority or competence to perform the control effectively.

Material weakness in internal control over compliance. A deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a compliance requirement will not be prevented, or detected and corrected, on a timely basis. In this section, a reasonable possibility exists when the likelihood of an event occurring is either reasonably possible or probable as defined as follows:

Reasonably possible. The chance of the future event or events occurring is more than remote but less than likely.

Probable. The future event or events are likely to occur.

Significant deficiency in internal control over compliance. A deficiency, or a combination of deficiencies, in internal control over compliance that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

Material noncompliance. In the absence of a definition of material noncompliance in the governmental audit requirement, a failure to follow compliance requirements or a violation of prohibitions included in the applicable compliance requirements that results in noncompliance that is quantitatively or qualitatively material, either individually or when aggregated with other noncompliance, to the affected government program.

Title 42 U.S. Code of Federal Regulations, Part 442, Standards for Payment to Nursing Facilities and Intermediate Care Facilities for Individuals with Intellectual Disabilities, states in part:

Section 442.109 – Certification period for ICF/IIDs: General Provisions

- (a) A survey agency may certify a facility that fully meets applicable requirements. The State Survey Agency must conduct a survey of each ICF/IID not later than 15 months after the last day of the previous survey.

Title 42 U.S. Code of Federal Regulations, Part 488, Survey, Certification, and Enforcement Procedures, states in part:

Section 488.28 – Providers or suppliers, other than Skilled Nursing Facilities (SNFs), Nursing Facilities (NFs), and Home Health Agencies (HHAs) with deficiencies

- (a) If a provider or supplier is found to be deficient in one or more of the standards in the conditions of participation, conditions for coverage, or conditions for certification or requirements, it may participate in, or be covered under, the Medicare program only if the provider or supplier has submitted an acceptable plan of correction for achieving compliance within a reasonable period of time acceptable to CMS. In the case of an immediate jeopardy situation, CMS may require a shorter time period for achieving compliance.
- (b) The existing deficiencies noted either individually or in combination neither jeopardize the health and safety of patients nor are of such character as to seriously limit the provider's capacity to render adequate care.
- (c) (1) If it is determined during a survey that a provider or supplier is not in compliance with one or more of the standards, it is granted a reasonable time to achieve compliance.
(2) The amount of time depends upon the -
 - (i) Nature of the deficiency; and
 - (ii) State survey agency's judgment as to the capabilities of the facility to provide adequate and safe care.
- (d) Ordinarily a provider or supplier is expected to take the steps needed to achieve compliance within 60 days of being notified of the deficiencies but the State survey agency may recommend that additional time be granted by the Secretary in individual situations, if in its

judgment, it is not reasonable to expect compliance within 60 days, for example, a facility must obtain the approval of its governing body, or engage in competitive bidding.

The Centers for Medicare and Medicaid Services, State Operations Manual, Chapter 2 – The Certification Process, states in part:

2138G – Schedule for Recertification

(Rev. 91, Issued: 09-27-13, Effective: 09-27-13, Implementation: 09-27-13)

The SA completes a recertification survey an average of every 12 months and at least once every 15 months (see §2141).

2141 – Recertification – ICFs/IID

(Rev. 91, Issued: 09-27-13, Effective: 09-27-13, Implementation: 09-27-13)

- The regulation at §442.15 provides that provider agreements for ICF/IID's would remain in effect as long as the facility remains in compliance with the Conditions of Participation (COP's). Regulations at §442.109 through §442.111.
- Beginning on May 16, 2012, ICF/IID's are no longer subject to time-limited agreements. However, they are to be surveyed for re-certification an average of every 12 months and at least once every 15 months.
- If during a survey the survey agency finds a facility does not meet the standards for participation the facility may remain certified if the survey agency makes two determinations – The facility may maintain its certification if the survey agency finds Immediate Jeopardy doesn't exist, and if the facility provides an acceptable plan of correction.
- An ICF/IID may be decertified under procedures outlined in Section 3012 of the State Operations Manual. More specifically, a facility may be decertified if an immediate jeopardy finding remains unabated after 23 days or if it fails to regain compliance with conditions of participation after 90 days.

ICF/IID's will be subject to survey an average of every 12 months and at least every 15 months, the same period that is applied to Nursing Homes.

The Department of Social and Health Services, Residential Care Services Division *Standard Operating Procedure: Intermediate Care Facilities for Individuals with Intellectual Disabilities (ICF/IID) – Plan of Correction*, states in part:

The Department will review the POC within five working days of receipt and will verify if the POC is acceptable.

Procedure

B. Off-site POC Review – the ICF program staff will:

1. Review the POC within five working days of receipt and confirm the POC for each deficiency includes:
 - a. How the facility will correct the deficiency as it relates to the resident;
 - b. How the facility will act to protect residents in similar situations;
 - c. Measures the facility will take or the systems it will alter to ensure that the problem does not recur;

- d. How the facility plans to monitor its performance to make sure that solutions are sustained;
- e. Dates when the corrective action will be completed (no more than 45 days from the last day of inspection for an ICF/IID that carries an Assisted Living or Nursing Home license and 60 days for a state Residential Habilitation Center (RHC));
- f. The title of the person or persons responsible to ensure correction for each deficiency

2018-053 The Department of Social and Health Services, Aging and Long-Term Support Administration, did not have adequate internal controls to ensure it complied with survey requirements for Medicaid nursing home facilities.

Federal Awarding Agency: U.S. Department of Health and Human Services
Pass-Through Entity: None
CFDA Number and Title: 93.775 State Medicaid Fraud Control Units
93.777 State Survey and Certification of Health Care Providers and Suppliers (Title XVIII) Medicare
93.778 Medical Assistance Program (Medicaid; Title XIX)
Federal Award Number: 1805WA5MAP; 1805WA5ADM; 1805WAIMPL; 1805WAINCT
Applicable Compliance Component: Special Tests and Provisions – Provider Health and Safety Standards
Known Questioned Cost Amount: None

Background

Medicaid is a jointly funded state and federal partnership providing coverage for about 1.9 million eligible low-income Washington residents who otherwise might go without medical care. Medicaid is Washington’s largest public assistance program and accounts for about one-third of the State’s federal expenditures. The program spent about \$12.7 billion in federal and state funds during fiscal year 2018.

The state Medicaid program spent about \$17.3 million to certify health care providers, including hospitals, home health agencies, intermediate care facilities, and nursing facilities in fiscal year 2018. Of this amount, the Department of Social and Health Services (Department) spent about \$6.6 million certifying nursing facilities. The State had 222 nursing facilities that were Medicare and/or Medicaid certified.

Residential Care Services, under the Department’s Aging and Long-Term Support Administration, is the state nursing home survey agency for Washington.

The survey for certifying a nursing facility is a resident-centered inspection that gathers information about the quality of service furnished in a facility to determine compliance with the requirements for participation. The survey focuses on the nursing home’s administration and patient services. The survey also assesses compliance with federal health, safety and quality standards designed to ensure patients receive safe and quality care services.

The Centers for Medicare and Medicaid Services (CMS) requires the state to complete standard surveys within 15.9 months after the previous survey, and the statewide average must not exceed 12.9 months for nursing facilities. If a survey uncovers deficiencies, the Department must deliver a Statement of Deficiency to the facility within 10 working days of the survey date. The facility must then submit a

Plan of Correction that the Department determines is acceptable within 60 calendar days of receipt, or risk forfeiting its Medicaid certification.

In prior audits, we reported the Department did not have adequate internal controls to ensure surveys were conducted timely and that follow-up on deficiencies were conducted in a timely manner. The prior finding numbers were 2017-043, 2016-036, 2015-044 and 2014-046.

Description of Condition

The Department did not have adequate internal controls to ensure it complied with survey requirements for Medicaid nursing home facilities.

The Department complied with federal regulations that require the Department to survey nursing homes every 15.9 months and meet a statewide average of 12.9 months. However, the Department did not ensure all Statement of Deficiencies were submitted to nursing facilities in a timely manner.

We used a statistical sampling method to randomly select and examine 21 of 203 nursing home surveys completed during the audit period. We found two instances (10 percent) when the Department did not deliver Statements of Deficiencies within 10 working days as required.

We consider this internal control deficiency to be a material weakness.

Cause of Condition

In its corrective action plan developed in response to the prior audit finding, the Department listed corrective measures it planned to resolve the internal control deficiency. The Department reported the corrective measures were completed as of February 2018. This audit again identified the Department did not comply with federal requirements, which indicates the corrective action was not entirely effective.

The Department had procedures in place to ensure that standard surveys are completed promptly. It is up to regional field survey and investigative staff to ensure a provider has achieved compliance through follow-up reviews, phone calls and/or visits.

The delays for sending the Statement of Deficiencies were due to regional administrative review of the deficiencies to ensure technical accuracy in the documents, achieving compliance with principles of documentation. With the implementation of the electronic Plan of Correction (ePOC) system in April 2017, the Department electronically distributed Statements of Deficiencies to nursing facilities in addition to submitting a written Statement of Deficiency upon the facility's request. In one case, the field manager responsible for the Nursing Facility Survey Unit attempted to submit the Statement of Deficiencies on the 10th working day after the survey, as required. However, a system outage prevented the Department from sending the Statement of Deficiencies until the following working day, when system functionality was restored.

Effect of Condition

When the Department does not send Statements of Deficiencies in a timely manner, the provider and/or facility cannot begin the development and submission of an acceptable Plan of Correction. This further prevents the Department from following up on deficiencies.

Recommendations

We recommend the Department strengthen internal controls to ensure Statements of Deficiencies are submitted within 10 working days after completing the initial survey.

Department's Response

The Department does not concur with the finding.

The Department does not concur that we do not have adequate internal controls over Statement of Deficiencies (SOD) being mailed by the 10th working day after survey exit. The internal controls that are in place have resulted in a decrease in exceptions from ten exceptions in FY16, to three exceptions in FY17, and two exceptions in FY18.

For one exception, the Electronic Plan of Correction (ePOC) system that the Department uses to deliver SODs to providers failed on the provider end, resulting in the Department manually delivering the SOD on the 11th day. For the second exception, administrative review of the SOD for accuracy resulted in the Department delivering the SOD on the 11th day. Both 11th day deliveries were less than 24 hrs beyond the federal requirement. The providers submitted their plans of correction timely with no impacts from the one-day delay.

System failures and administrative review are acceptable reasons providers may not receive their SODs on the 10th day. Computer technicalities and federal system failures are beyond the control of the Department. Administrative review is necessary to ensure a complete, accurate and appropriate SOD.

The Department has confirmed that the technical difficulties of receiving SODs via ePOC has been resolved for the provider in question. The Department will continue to use internal controls and quality assurance reviews to monitor the timeliness of SOD distribution to providers.

Auditor's Concluding Remarks

There is no latitude in the federal requirement regarding the State's responsibility to issue Statement of Deficiencies within 10 working days of the exit date. The Department issued the Statement of Deficiencies beyond 10 working days of the exit date. The regulations do not give leeway to submit a Statement Deficiency on the 11th day. The regulations do give leeway from day one to day 10.

We reaffirm our finding and will review the status of the Department's corrective action during our next audit.

Applicable Laws and Regulations

Title 2 U.S. Code of Federal Regulations Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance) establishes the following applicable requirements:

Section 200.303 Internal controls, states in part:

The non-Federal entity must:

- (a) Establish and maintain effective internal control over the Federal award that provides reasonable assurance that the non-Federal entity is managing the Federal award in compliance with Federal statutes, regulations, and the terms and conditions of the Federal award. These internal controls should be in compliance with guidance in “Standards for Internal Control in the Federal Government” issued by the Comptroller General of the United States or the “Internal Control Integrated Framework”, issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).

Section 200.516 Audit findings, states in part:

- (a) *Audit findings reported.* The auditor must report the following as audit findings in a schedule of findings and questioned costs:
 - (1) Significant deficiencies and material weaknesses in internal control over major programs and significant instances of abuse relating to major programs. The auditor’s determination of whether a deficiency in internal control is a significant deficiency or material weakness for the purpose of reporting an audit finding is in relation to a type of compliance requirement for a major program identified in the Compliance Supplement.

The American Institute of Certified Public Accountants defines significant deficiencies and material weaknesses in internal controls over compliance in its *Codification of Statements on Auditing Standards*, section 935, Compliance Audits, as follows:

.11 For purposes of adapting GAAS to a compliance audit, the following terms have the meanings attributed as follows: ...

Deficiency in internal control over compliance. A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance on a timely basis. A deficiency in design exists when (a) a control necessary to meet the control objective is missing, or (b) an existing control is not properly designed so that, even if the control operates as designed, the control objective would not be met. A deficiency in operation exists when a properly designed control does not operate as designed or the person performing the control does not possess the necessary authority or competence to perform the control effectively.

Material weakness in internal control over compliance. A deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a compliance requirement will not be prevented, or

detected and corrected, on a timely basis. In this section, a reasonable possibility exists when the likelihood of an event occurring is either reasonably possible or probable as defined as follows:

Reasonably possible. The chance of the future event or events occurring is more than remote but less than likely.

Probable. The future event or events are likely to occur.

Significant deficiency in internal control over compliance. A deficiency, or a combination of deficiencies, in internal control over compliance that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

Centers for Medicare and Medicaid Services, State Operations Manual, Chapter 2 – The Certification Process, states in part:

2728 – Statement of Deficiencies and Plan of Correction, Form CMS-2567

The SA mails the provider/supplier a copy of Form CMS-2567 within 10 working days after the survey. If there are deficiencies, the SA allows the provider/supplier 10 calendar days to complete and return the PoC.

2018-054 The Department of Social and Health Services, Aging and Long-Term Support Administration, did not have adequate internal controls over and did not comply with requirements to ensure Medicaid payments to home care agencies were allowable.

Federal Awarding Agency:	U.S. Department of Health and Human Services
Pass-Through Entity:	None
CFDA Number and Title:	93.775 State Medicaid Fraud Control Units 93.777 State Survey and Certification of Health Care Providers and Suppliers (Title XVIII) Medicare 93.778 Medical Assistance Program (Medicaid; Title XIX)
Federal Award Number:	1805WA5MAP; 1805WA5ADM; 1805WAIMPL; 1805WAINCT
Applicable Compliance Component:	Activities Allowed/Unallowed Cost Principles
Known Questioned Cost Amount:	\$8,315

Background

Medicaid is a jointly funded state and federal partnership providing coverage for about 1.9 million eligible low-income Washington residents who otherwise might go without medical care. Medicaid is Washington’s largest public assistance program and accounts for about one-third of the State’s federal expenditures. The program spent about \$12.7 billion in federal and state funds during fiscal year 2018.

The Department of Social and Health Services (Department) offers personal care, respite and other services to support Medicaid clients in community settings. The Department uses an assessment to evaluate a client’s support needs and to calculate the number of personal care hours the client needs to successfully live in the community.

Clients have two options to choose from for the delivery of their personal care services. One option is to have the services provided by a home care aide who is recruited, trained, employed and supervised by a home care agency. The other option is for the client to recruit, hire and supervise their own provider. This type of employee is referred to as an individual provider.

State law prohibits the Department from paying home care agencies if the agency does not verify employee hours by an electronic timekeeping method. Electronic timekeeping is defined as an electronic, verifiable method of recording an employee’s presence with the client at the beginning and end of the employee’s client visit.

The Department also has a policy that requires home care agency employees to complete a task list at the end of every visit and requires that list to be initialed by the client or the client’s representative to verify the personal care tasks that were provided.

Home care agencies are contracted with the Department through the state's 13 Area Agencies on Aging (AAA). The Department pays AAAs to monitor the home care agencies for contractual compliance in many areas, including verification of time and task performance. The Department monitors the AAAs to ensure they:

- Use the Department's prescribed monitoring tool
- Have written policies and procedures around their monitoring practices
- Conduct annual provider risk assessments
- Annually monitor providers to ensure compliance with applicable laws and regulations
- Test for required provider licenses and certifications
- Have a standard process for handling complaints about providers and follow-up procedures
- Determine if provider corrective action was appropriate and progress toward corrective action was reviewed

The Department paid about \$368 million to home care agencies for personal care services provided to clients in fiscal year 2018.

Description of Condition

The Department's Aging and Long-Term Support Administration did not have adequate internal controls over and did not comply with requirements to ensure Medicaid payments to home care agencies were allowable.

The Department did not adequately monitor the AAAs to ensure home care agencies completed and maintained electronic timekeeping records and task lists to support payments made to home care agencies.

We consider this internal control deficiency to be a material weakness.

This condition was not reported in the prior audit.

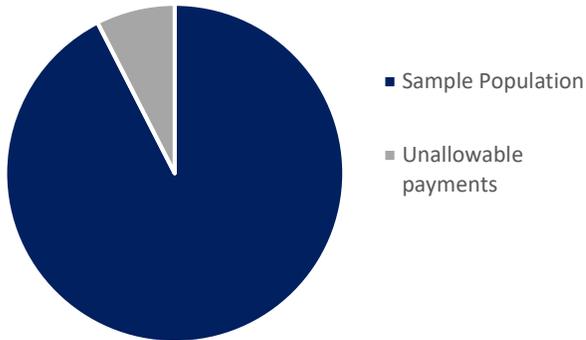
Cause of Condition

The Department did not monitor to the level of detail needed to gain assurance that home care agencies completed and maintained task lists used to verify personal care services were delivered to clients.

Effect of Condition and Questioned Costs

By not ensuring home care agencies complete and maintain adequate supporting documentation for time and task performance for its employees, the Department increases the risk of making improper payments to providers.

Unallowable monthly payments



Using a statistical sampling method, we randomly selected 86 monthly payments made to home care agencies from a population of 213,543. The cost of these payments totaled \$242,876

We requested electronic timekeeping records and task lists from home care agencies for each day during the selected months.

We found seven of the 86 monthly payments were not supported by adequate documentation.

Specifically, we found:

- 25 instances when a daily payment (one month) was not supported by an electronic timekeeping record and the hours paid were not supported
- 28 instances when a daily payment was not supported by a task list
- 62 instances when a daily task list was not signed by the client or their representative indicating services were received

These instances included a home care agency that claimed 25 daily payments during one month but subsequently closed and did not respond to our request for supporting documentation.

The cost of the daily payments that were not supported by adequate documentation was \$14,849. The federal share of these questioned costs was \$8,315. Because a statistical sampling method was used to select the payments we examined, we estimate the likely improper payments to be \$34,029,614. The federal share of the likely improper payments is \$19,056,584.

	Known questioned costs	Likely improper payments
Federal expenditures	\$8,315	\$19,056,584
State expenditures	\$6,533	\$14,973,030
Total expenditures	\$14,849	\$34,029,614

The statistical sample used for testing was also used to test compliance with other activities allowed requirements. Because some unallowable payments we examined violated multiple areas of activities allowed some of the questioned costs reported here might also be reported in finding numbers 2018-059 and 2018-060.

We question costs when we find an agency has not complied with grant regulations or when it does not have adequate documentation to support its expenditures.

Our sampling methodology meets statistical sampling criteria under generally accepted auditing standards in AU-C 530.05. It is important to note that the sampling technique we used is intended to

support our audit conclusions by determining if expenditures complied with program requirements in all material respects. Accordingly, we used an acceptance sampling formula designed to provide a high level of assurance, with a 95 percent confidence of whether exceptions exceeded our materiality threshold. Our audit report and finding reflects this conclusion. However, the likely improper payment projections are a point estimate and only represent our “best estimate of total questioned costs” as required by 2 CFR 200.516(3). To ensure a representative sample, we stratified the population by dollar amount.

Recommendations

We recommend the Department:

- Improve its monitoring of AAAs to ensure home care agencies maintain required documentation to support payments
- Consult with the U.S. Department of Health and Human Services to discuss whether the questioned costs identified in the audit should be repaid

Department’s Response

The Department partially concurs with the finding.

The Department concurs that there were 25 instances when a daily payment was not supported by an electronic timekeeping record due to the home care agency closing and not responding to the request. The Department will modify the tool it utilizes to monitor AAAs to specifically review that AAAs are monitoring home care agency’s compliance with electronic timekeeping contractual requirements.

The Department agrees that there were missing, or no initials on task sheets, but does not concur with the SAO’s conclusion that this should result in questioned cost as task sheets are not required by federal or state law. Task sheets are required by the home care agency contract and are used to document what tasks were completed during the provider’s shift. If task sheets are not completed the home care agency will be required to develop a corrective action plan.

The Department will work with AAA contract management staff to request corrective action plans from home care agencies that are noncompliant with contractual requirements.

Auditor’s Concluding Remarks

The Department’s Home Care Agency Statement of Work (attached to Department of Social and Health Services AAA agreement), states in part that a task sheet verifying task performance shall be kept for every client under the Medicaid funded programs served by the Contractor and must clearly indicate what tasks were completed/performed during each home visit. This documentation provides evidence that the services provided were allowable to be reimbursed by Medicaid.

We reaffirm our finding and will review the status of the Department’s corrective action during our next audit.

Applicable Laws and Regulations

Title 2 U.S. Code of Federal Regulations Part 200, Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards (Uniform Guidance) establishes the following applicable requirements:

Section 200.53 Improper Payments states:

- (a) *Improper payment* means any payment that should not have been made or that was made in an incorrect amount (including overpayments and underpayments) under statutory, contractual, administrative, or other legally applicable requirements; and
- (b) *Improper payment* includes any payment to an ineligible party, any payment for an ineligible good or service, any duplicate payment, any payment for a good or service not received (except for such payments where authorized by law), any payment that does not account for credit for applicable discounts, and any payment where insufficient or lack of documentation prevents a reviewer from discerning whether a payment was proper.

Section 200.303 Internal controls, states in part:

The non-Federal entity must:

- (a) Establish and maintain effective internal control over the Federal award that provides reasonable assurance that the non-Federal entity is managing the Federal award in compliance with Federal statutes, regulations, and the terms and conditions of the Federal award. These internal controls should be in compliance with guidance in “Standards for Internal Control in the Federal Government” issued by the Comptroller General of the United States or the “Internal Control Integrated Framework”, issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).
- (b) Comply with Federal statutes, regulations, and the terms and conditions of the Federal awards.
- (d) Take prompt action when instances of noncompliance are identified including noncompliance identified in audit findings.

Section 200.403 Factors affecting Allowability of costs.

Except where otherwise authorized by statute, costs must meet the following general criteria in order to be allowable under Federal awards.

- (a) Be necessary and reasonable for the performance of the Federal award and be allocable thereto under these principles.
- (b) Conform to any limitations or exclusions set forth in these principles or in the Federal award as to types or amount of cost items.
- (c) Be consistent with policies and procedures that apply uniformly to both federally-financed and other activities of the non-Federal entity.
- (d) Be accorded consistent treatment. A cost may not be assigned to a Federal award as a direct cost if any other cost incurred for the same purpose in like circumstances has been allocated to the Federal award as an indirect cost.
- (e) Be determined in accordance with generally accepted accounting principles (GAAP), except, for state and local governments and Indian tribes only, as otherwise provided for in this part.

- (f) Not be included as a cost or used to meet cost sharing or matching requirements of any other federally-financed program in either the current or a prior period. See also §200.306 Cost sharing or matching paragraph (b).
- (g) Be adequately documented. See also §§200.300 Statutory and national policy requirements through 200.309 Period of performance of this part.

Section 200.410 Collection of unallowable costs.

Payments made for costs determined to be unallowable by either the Federal awarding agency, cognizant agency for indirect costs, or pass-through entity, either as direct or indirect costs, must be refunded (including interest) to the Federal Government in accordance with instructions from the Federal agency that determined the costs are unallowable unless Federal statute or regulation directs otherwise. See also Subpart D— Post Federal Award Requirements of this part, §§200.300 Statutory and national policy requirements through 200.309 Period of performance.

Section 200.516 Audit findings, states in part:

- (a) *Audit findings reported.* The auditor must report the following as audit findings in a schedule of findings and questioned costs:
 - (1) Significant deficiencies and material weaknesses in internal control over major programs and significant instances of abuse relating to major programs. The auditor's determination of whether a deficiency in internal control is a significant deficiency or material weakness for the purpose of reporting an audit finding is in relation to a type of compliance requirement for a major program identified in the Compliance Supplement.
 - (2) Material noncompliance with the provisions of Federal statutes, regulations, or the terms and conditions of Federal awards related to a major program. The auditor's determination of whether a noncompliance with the provisions of Federal statutes, regulations, or the terms and conditions of Federal awards is material for the purpose of reporting an audit finding is in relation to a type of compliance requirement for a major program identified in the compliance supplement.
 - (3) Known questioned costs that are greater than \$25,000 for a type of compliance requirement for a major program. Known questioned costs are those specifically identified by the auditor. In evaluating the effect of questioned costs on the opinion on compliance, the auditor considers the best estimate of total costs questioned (likely questioned costs), not just the questioned costs specifically identified (known questioned costs). The auditor must also report known questioned costs when likely questioned costs are greater than \$25,000 for a type of compliance requirement for a major program. In reporting questioned costs, the auditor must include information to provide proper perspective for judging the prevalence and consequences of the questioned costs.

The American Institute of Certified Public Accountants defines significant deficiencies and material weaknesses in internal controls over compliance in its *Codification of Statements on Auditing Standards*, section 935, Compliance Audits, as follows:

.11 For purposes of adapting GAAS to a compliance audit, the following terms have the meanings attributed as follows: ...

Deficiency in internal control over compliance. A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance on a timely basis. A deficiency in design exists when (a) a control necessary to meet the control objective is missing, or (b) an existing control is not properly designed so that, even if the control operates as designed, the control objective would not be met. A deficiency in operation exists when a properly designed control does not operate as designed or the person performing the control does not possess the necessary authority or competence to perform the control effectively.

Material weakness in internal control over compliance. A deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a compliance requirement will not be prevented, or detected and corrected, on a timely basis. In this section, a reasonable possibility exists when the likelihood of an event occurring is either reasonably possible or probable as defined as follows:

Reasonably possible. The chance of the future event or events occurring is more than remote but less than likely.

Probable. The future event or events are likely to occur.

Significant deficiency in internal control over compliance. A deficiency, or a combination of deficiencies, in internal control over compliance that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

Material noncompliance. In the absence of a definition of material noncompliance in the governmental audit requirement, a failure to follow compliance requirements or a violation of prohibitions included in the applicable compliance requirements that results in noncompliance that is quantitatively or qualitatively material, either individually or when aggregated with other noncompliance, to the affected government program.

Office of Management and Budget OMB Uniform Guidance, Compliance Supplement for 2017, *Part 4 – Agency Program Requirements*, 4.93.778 *Medicaid Cluster*, states in part:

General Audit Approach for Medicaid Payments

To be allowable, Medicaid costs for medical services must be (1) covered by the State plan and waivers; (2) reviewed by the State consistent with the State’s documented procedures and system for determining medical necessity of claims; (3) properly coded; and (4) paid at the rate allowed by the State plan. Additionally, Medicaid costs must be net of beneficiary cost-sharing obligations and applicable credits (e.g., insurance, recoveries from other third parties who are

responsible for covering the Medicaid costs, and drug rebates), paid to eligible providers, and only provided on behalf of eligible individuals.

Revised Code of Washington 74.39A.325

In-home personal care or respite services—Electronic timekeeping.

- (1) The department shall not pay a home care agency licensed under chapter 70.127 RCW for in-home personal care or respite services provided under this chapter, Title 71A RCW, or chapter 74.39 RCW if the home care agency does not verify agency employee hours by electronic timekeeping except in circumstances where electronic verification is not possible as verified by the home care agency.
- (2) For purposes of this section, "electronic timekeeping" means an electronic, verifiable method of recording an employee's presence with the client at the beginning and end of the employee's client visit shift.

Home and Community Services Management Bulletin – H10-008 Procedure, states in part:

The task sheet or home visit sheet must be initialed by the client or their representative at the end of every visit for verification of personal care tasks completed or respite services provided.

Department of Social and Health Services AAA agreement (contract with home care agencies), states in part:

16. Maintenance of Records. During the term of this agreement and for six (6) years following termination or expiration of this Agreement, both parties shall maintain records sufficient to:
 - a. Document performance of all acts required by law, regulation, or this Agreement;
 - b. Demonstrate accounting procedures, practices, and records that sufficiently and properly document the AAA's invoices to DSHS and all expenditures made by the AAA to perform as required by this Agreement.

Home Care Agency Statement of Work (attached to Department of Social and Health Services AAA agreement), states in part:

H. Verification of time and task performance

The home care agency must maintain all records related to electronic timekeeping, alternative verification, or manual corrections and provide these records to the appropriate department or designee staff for review when requested.

A form (task sheet) verifying task performance shall be kept for every client under the Medicaid funded programs served by the Contractor and must clearly indicate what tasks were completed/performed during each home visit.

2018-055

The Department of Social and Health Services did not ensure the federal portion of uncashed Medicaid checks was returned to its grantor.

Federal Awarding Agency: U.S. Department of Health and Human Services
Pass-Through Entity: None
CFDA Number and Title: 93.775 State Medicaid Fraud Control Units
93.777 State Survey and Certification of Health Care Providers and Suppliers (Title XVIII) Medicare
93.778 Medical Assistance Program (Medicaid; Title XIX)
Federal Award Number: 1805WA5MAP; 1805WA5ADM; 1805WAIMPL; 1805WAINCT
Applicable Compliance Component: Activities Allowed/Unallowed Allowable Costs/Cost Principles
Known Questioned Cost Amount: \$237,078

Background

Medicaid is a jointly funded state and federal partnership providing coverage for about 1.9 million eligible low-income Washington residents who otherwise might go without medical care. Medicaid is Washington's largest public assistance program and accounts for about one-third of the State's federal expenditures. The program spent about \$12.7 billion in federal and state funds during fiscal year 2018.

The Department of Social and Health Services (Department) serves over 37,000 clients who receive services from individual providers through a variety of state plan, waiver and state-only programs. The majority of client services are funded through the Community First Choice (CFC) program. Services include assisting clients with personal care services, providing transportation, respite and relief care and client skills acquisition. The goal of the programs is to support clients in their homes so they can continue to live in their communities and avoid institutional care.

Clients receive a set number of personal care hours each month based on a Department assessment. About 45,000 individual providers contract with the Department to provide personal care services and are paid through a payroll system known as Individual ProviderOne (IPOne). This system is managed and maintained by a vendor.

Before each pay date, the vendor sends the Department a request for the total amount of the payroll cost. The Department funds the request using federal Medicaid and state dollars. Generally, the vendor pays individual providers through electronic fund and debit card transfers, but also issues paper checks. Federal regulations require states to return the Medicaid-funded portion of uncashed checks to the grantor after 180 days.

Description of Condition

The Department of Social and Health Services did not ensure the federal portion of uncashed Medicaid checks were returned to its grantor.

In August 2018, we reported in an accountability audit finding that the Department did not return the federal portion of uncashed checks that were older than 180 days. The accountability audit report number was 1021987.

This condition was not reported in the prior single audit.

Cause of Condition

The Department said the vendor experienced significant staff turnover in the past few years and has not dedicated the necessary resources to adequately manage the system and implement an adjustment process that would allow it to return funds to the Department.

Effect of Condition

We reviewed the vendor's bank reconciliation as of June 30, 2018, and found the vendor had uncashed checks on its books dating back to April 1, 2016 – the date the payroll system began paying individual providers. We isolated the checks between April 1, 2016, and December 31, 2017. Checks issued after this date are within the 180-day allowance and not subject to return until after June 30, 2018.

We found a total of \$474,156 in uncashed checks that were over 180 days old as of June 30, 2018. Of that amount, at least \$237,078 (50 percent) was funded by Medicaid and had not been returned to the grantor. The vendor's payroll system is currently unable to make adjustments for uncashed checks and until the issue is resolved, the Department will not know the exact amount to refund to the grantor.

Type of expenditure	Known questioned costs
Federal	\$ 237,078
State	\$237,078
Total	\$474,156

The statistical sample used for testing in parts of the fiscal year 2018 Medicaid audit was used to test compliance with other activities allowed requirements. Because some unallowable payments we examined violated multiple areas of activities allowed some of the questioned costs reported here might also be reported in finding numbers 2018-050, 2018-051, 2018-056, 2018-059, and 2018-060.

We question costs when we find an agency has not complied with grant regulations or when it does not have adequate documentation to support its expenditures.

Recommendations

We recommend the Department:

- Work with its vendor to identify when checks go uncashed and return the federal share of the payment to the grantor
- Consult with the U.S. Department of Health and Human Services to discuss whether the questioned costs identified in the audit should be repaid

Department's Response

The Department concurs with the finding.

Due to contractor staffing and system issues, the contractor was not able to implement the uncashed check process. The Department and the contractor have worked together to develop the interface and process.

The code will be deployed in IPOne, in the 2019 Release 01 and the contractor will send over the outstanding uncashed checks to the Department, for April 2016 to current, by May 2019.

Auditor's Concluding Remarks

We thank the Department for its cooperation and assistance throughout the audit. We will review the status of the Department's corrective action during our next audit.

Applicable Laws and Regulations

Title 2 U.S. Code of Federal Regulations Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance) establishes the following applicable requirements:

Section 200.53 Improper Payments states:

- (a) *Improper payment* means any payment that should not have been made or that was made in an incorrect amount (including overpayments and underpayments) under statutory, contractual, administrative, or other legally applicable requirements; and
- (b) *Improper payment* includes any payment to an ineligible party, any payment for an ineligible good or service, any duplicate payment, any payment for a good or service not received (except for such payments where authorized by law), any payment that does not account for credit for applicable discounts, and any payment where insufficient or lack of documentation prevents a reviewer from discerning whether a payment was proper.

Section 200.403 Factors affecting Allowability of costs.

Except where otherwise authorized by statute, costs must meet the following general criteria in order to be allowable under Federal awards.

- (a) Be necessary and reasonable for the performance of the Federal award and be allocable thereto under these principles.
- (b) Conform to any limitations or exclusions set forth in these principles or in the Federal award as to types or amount of cost items.
- (c) Be consistent with policies and procedures that apply uniformly to both federally-financed and other activities of the non-Federal entity.
- (d) Be accorded consistent treatment. A cost may not be assigned to a Federal award as a direct cost if any other cost incurred for the same purpose in like circumstances has been allocated to the Federal award as an indirect cost.
- (e) Be determined in accordance with generally accepted accounting principles (GAAP), except, for state and local governments and Indian tribes only, as otherwise provided for in this part.
- (f) Not be included as a cost or used to meet cost sharing or matching requirements of any other federally-financed program in either the current or a prior period. See also §200.306 Cost sharing or matching paragraph (b).
- (g) Be adequately documented. See also §§200.300 Statutory and national policy requirements through 200.309 Period of performance of this part.

Section 200.410 Collection of unallowable costs.

Payments made for costs determined to be unallowable by either the Federal awarding agency, cognizant agency for indirect costs, or pass-through entity, either as direct or indirect costs, must be refunded (including interest) to the Federal Government in accordance with instructions from the Federal agency that determined the costs are unallowable unless Federal statute or regulation directs otherwise. See also Subpart D—Post Federal Award Requirements of this part, §§200.300 Statutory and national policy requirements through 200.309 Period of performance.

Section 200.516 Audit findings, states in part:

- (a) *Audit findings reported.* The auditor must report the following as audit findings in a schedule of findings and questioned costs:
 - (3) Known questioned costs that are greater than \$25,000 for a type of compliance requirement for a major program. Known questioned costs are those specifically identified by the auditor. In evaluating the effect of questioned costs on the opinion on compliance, the auditor considers the best estimate of total costs questioned (likely questioned costs), not just the questioned costs specifically identified (known questioned costs). The auditor must also report known questioned costs when likely questioned costs are greater than \$25,000 for a type of compliance requirement for a major program. In reporting questioned costs, the auditor must include information to provide proper perspective for judging the prevalence and consequences of the questioned costs.

Office of Management and Budget OMB Uniform Guidance, Compliance Supplement for 2017, *Part 4 – Agency Program Requirements, 4.93.778 Medicaid Cluster*, states in part:

General Audit Approach for Medicaid Payments

To be allowable, Medicaid costs for medical services must be (1) covered by the State plan and waivers; (2) reviewed by the State consistent with the State’s documented procedures and system for determining medical necessity of claims; (3) properly coded; and (4) paid at the rate allowed by the State plan. Additionally, Medicaid costs must be net of beneficiary cost-sharing obligations and applicable credits (e.g., insurance, recoveries from other third parties who are responsible for covering the Medicaid costs, and drug rebates), paid to eligible providers, and only provided on behalf of eligible individuals.

Title 42 U.S. Code of Federal Regulations Part 433 State Fiscal Administration, subpart A-Federal Matching and General Administration Provisions, states:

Section 433.40 Treatment of uncashed or cancelled (voided) Medicaid checks.

- (a) *Purpose*. This section provides the rules to ensure that States refund the Federal portion of uncashed or cancelled (voided) checks under title XIX.
- (b) *Definitions*. As used in this section—*Cancelled (voided) check* means a Medicaid check issued by a State or fiscal agent which prior to its being cashed is cancelled (voided) by the State or fiscal agent, thus preventing disbursement of funds.
Check means a check or warrant that a State or local agency uses to make a payment.
Fiscal agent means an entity that processes or pays vendor claims for the Medicaid State agency.
Uncashed check means a Medicaid check issued by a State or fiscal agent which has not been cashed by the payee.
Warrant means an order by which the State agency or local agency without the authority to issue checks recognizes a claim. Presentation of a warrant by the payee to a State officer with authority to issue checks will result in release of funds due.
- (c) *Refund of Federal financial participation (FFP) for uncashed checks*—(1) *General provisions*. If a check remains uncashed beyond a period of 180 days from the date it was issued; i.e., the date of the check, it will no longer be regarded as an allowable program expenditure. If the State has claimed and received FFP for the amount of the uncashed check, it must refund the amount of FFP received.
(2) *Report of refund*. At the end of each calendar quarter, the State must identify those checks which remain uncashed beyond a period of 180 days after issuance. The State agency must refund all FFP that it received for uncashed checks by adjusting the Quarterly Statement of Expenditures for that quarter. If an uncashed check is cashed after the refund is made, the State may file a claim. The claim will be considered to be an adjustment to the costs for the quarter in which the check was originally claimed. This claim will be paid if otherwise allowed by the Act and the regulations issued pursuant to the Act.
(3) If the State does not refund the appropriate amount as specified in paragraph (c)(2) of this section, the amount will be disallowed.

- (d) *Refund of FFP for cancelled (voided) checks*—(1) *General provision.* If the State has claimed and received FFP for the amount of a cancelled (voided) check, it must refund the amount of FFP received.
- (2) *Report of refund.* At the end of each calendar quarter, the State agency must identify those checks which were cancelled (voided). The State must refund all FFP that it received for cancelled (voided) checks by adjusting the Quarterly Statement of Expenditures for that quarter.
- (3) If the State does not refund the appropriate amount as specified in paragraph (d)(2) of this section, the amount will be disallowed.

2018-056 **The Department of Social and Health Services, Aging and Long-Term Support Administration, did not have adequate internal controls to ensure all Medicaid Community First Choice individual providers had proper background checks.**

U.S. Department of Health and Human Services

Federal Awarding Agency:

Pass-Through Entity:

None

CFDA Number and Title:

93.775 State Medicaid Fraud Control Units
93.777 State Survey and Certification of Health Care
 Providers and Suppliers (Title XVIII)
 Medicare
93.778 Medical Assistance Program (Medicaid;
 Title XIX)

Federal Award Number:

1805WA5MAP; 1805WA5ADM;
1805WAIMPL; 1805WAINCT

Applicable Compliance Component:

Activities Allowed/Unallowed
Allowable Costs/Cost Principles

Known Questioned Cost Amount:

\$25,288

Background

Medicaid is a jointly funded state and federal partnership providing coverage for about 1.9 million eligible low-income Washington residents who otherwise might go without medical care. Medicaid is Washington's largest public assistance program and accounts for about one-third of the State's federal expenditures. The program spent about \$12.7 billion in federal and state funds during fiscal year 2018.

The Aging and Long-Term Care Administration at the Department of Social and Health Services (Department) offers personal care and other services to support Medicaid clients in community settings through the Community First Choice program. The Department uses an assessment to evaluate a client's support needs and to calculate the number of personal care hours the client is eligible to receive in the community. Individual providers contract with the Department to provide personal care services to clients through one of the 13 Area Agency on Aging (AAA) offices across the state. AAA's work with providers and clients in their area to ensure providers are meeting eligibility requirements and clients are having their needs met

In fiscal year 2018, the state Medicaid program spent about \$1.1 billion on Community First Choice personal care services.

Medicaid is the primary funding source for long-term care providers. The Medicaid Home and Community Based Services program permits states to furnish long-term care services to Medicaid clients in home and community settings. These services are provided to clients in their home by individuals or agencies chosen by the Medicaid client or the client's legal representative. Payments to individual providers contracted with the Aging and Long-Term Support Administration accounted for more than 6 percent of all Medicaid payments made in fiscal year 2018.

Individual providers are paid an hourly rate for providing personal care and a mileage rate for providing transportation services to their clients. Individual providers use the Department's Individual ProviderOne (IPOne) system to invoice the Department for their hourly service and mileage claims.

State law (RCW 43.43.837) requires that all individual providers must meet the basic qualifications to provide services to Medicaid clients, which include being at least 18 years old, passing background checks, and receiving required certifications and training. Individual providers must complete a Washington background check every two years and, effective January 8, 2012, all new contracted providers or applicants who have not lived in Washington for three consecutive years must complete a national fingerprint-based background check. Some clients choose to receive care from their parent or legal guardian. If the parent or legal guardian had a contract in place prior to January 7, 2012, a fingerprint background check is not required..

The Department's Secretary establishes a list of crimes that automatically disqualify people from having unsupervised access to vulnerable clients. This list was referred to as "the Secretary's List," but has been incorporated into regulation (Washington Administrative Code 388-113). People who commit a crime listed in State rule are automatically prohibited from "licensing, contracting, certification, or from having unsupervised access to children, vulnerable adults or to individuals with a developmental disability."

If a person is found to have committed a crime not listed in State rule, they are not automatically disqualified from having unsupervised access to vulnerable clients. The provider must receive a Character, Competence and Suitability review to assess and determine if they or their employees may have unsupervised access to clients.

The Department performs an annual quality review of AAA offices, which includes reviewing provider files to ensure they comply with provider eligibility requirements. A proficiency rate is issued for each of the questions that is answered as part of the review. Proficiency rates that fall below 86 percent require the AAA to submit a proficiency improvement plan (PIP) to respond to the deficiencies that were identified and how it plans to correct them. The Department then reviews the plan to ensure it will correct the deficiencies before approving the plan.

In prior audits, we reported the Department made payments on behalf of individual providers without valid background checks. The prior finding numbers were 2017-049, 2016-040, 2015-040, 2014-049, 2013-40, 12-41 and 11-34.

Description of Condition

The Department did not have adequate internal controls to ensure all Medicaid Community First Choice individual providers had proper background checks.

We examined the PIPs for three of the AAA offices that had a proficiency rate that fell below 86 percent. For two (66.7 percent) of the three PIPs, we noted the AAA did not address how it would correct the background check deficiency.

We consider this internal control deficiency to be a material weakness.

This internal control deficiency was not reported in the prior audit.

Cause of Condition

The Department's proficiency improvement plans contain several quality assurance questions. Due to lack of staff oversight, the background check question was inadvertently left off the proficiency improvement plans for two AAAs. This in turn, led to background checks not being included as corrective actions.

Effect of Condition and Questioned Costs

Providers who do not meet the background check requirements are not eligible to provide services to Medicaid clients. Any payments made by the Department to ineligible providers are unallowable.

We used a statistical sampling method to randomly select and examine 132 of 32,401 Community First Choice individual providers who provided in-home care services to in-home clients during fiscal year 2018 to ensure:

- A proper background check had been completed within the past two years
- No individuals with disqualifying crimes listed in State rule provided care to vulnerable adult clients at the time of the audit, or during the month(s) when the Department paid them
- Providers who had committed crimes that were not listed as disqualifying in State rule passed a Character, Competence and Suitability review permitting them to work unsupervised with vulnerable adults
- The entire period when the provider had access to Medicaid clients was covered by a Washington background check and, if required, a national fingerprint background check

We found:

- Five instances when the Department did not perform a fingerprint background check of a provider. Although a Washington background check was conducted on these providers, State law required a fingerprint check also be completed
- One instance when the Department did not promptly perform a Washington background check at the time of renewal

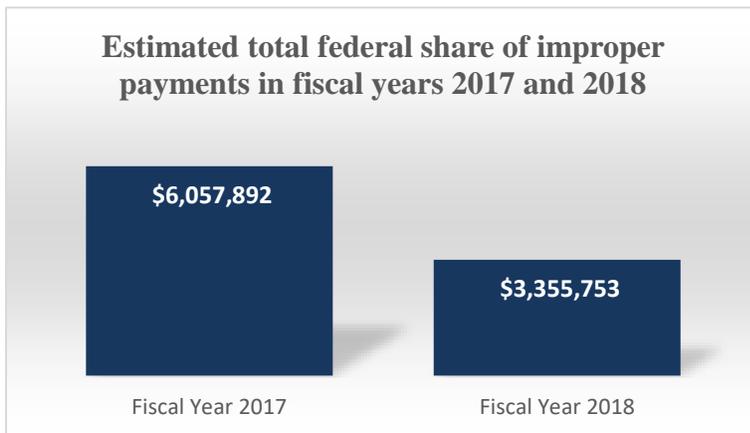
We also performed follow-up testing on our 2017 audit finding that identified one instance when the Department did not perform a fingerprint background check on a provider as required. We found the Department terminated the provider's contract in March 2018.

Direct service costs for 2017 and 2018			
Description	Number of exceptions	Total paid	Federal share
Did not perform a fingerprint background check	5	\$26,809	\$15,013
Did not promptly perform a Washington background check at the time of renewal	1	\$0	\$0
Did not perform a fingerprint background check - prior year individual provider	1	\$7,020	\$3,931
Totals	7	\$33,829	\$18,944

We determined the Department made \$33,829 in unallowable payments to providers for direct services to clients. We are questioning \$18,944, which is the federal portion of the unallowable payments.

When unallowable payments are identified, federal regulations suggest auditors consider if associated costs, such as benefits, were also paid. The Department pays payroll related benefits, which are considered associated costs, on behalf of Community First Choice providers. Examples of these costs include health insurance, retirement, payroll taxes and training.

For the \$33,829 in payments determined were unallowable, we identified \$11,501 in associated costs that we also consider to be unallowable. We are questioning \$6,344, which is the federal portion of the unallowable payments related to associated costs. The Department contracts with a vendor that manages IPOne. The system is currently unable to make overpayment adjustments and until the issue is resolved, the Department will not know the exact amount of associated costs to refund the grantor. In addition, the system has been unable to correctly calculate State Unemployment Tax Act (SUTA) taxes



since it began processing payroll on April 1, 2016.

Because a statistical sampling method was used to select the Community First Choice individual providers that we examined, we estimate the amount of likely improper payments to be \$6,015,778. The federal share of this estimate is \$3,355,753.

The statistical sample used for testing was also used to test compliance with other activities allowed requirements. Because some unallowable payments we examined violated multiple areas of activities allowed some of the questioned costs reported here might also be reported in finding numbers 2018-050, 2018-051, 2018-055, 2018-059 and 2018-060.

Projection to population	Known questioned costs	Likely improper payments
Federal expenditures	\$25,288	\$3,355,753
State expenditures	\$20,042	\$2,660,025
Total expenditures	\$45,330	\$6,015,778

We question costs when we find an agency has not complied with grant regulations or when it does not have adequate documentation to support its expenditures.

Our sampling methodology meets statistical sampling criteria under generally accepted auditing standards in AU-C 530.05. It is important to note that the sampling technique we used is intended to support our audit conclusions by determining if expenditures complied with program requirements in all material respects. Accordingly, we used an acceptance sampling formula designed to provide a very high level of assurance, with a 99 percent confidence of whether exceptions exceeded our materiality threshold. Our audit report and finding reflects this conclusion. However, the likely improper payment projections are a point estimate and only represent our “best estimate of total questioned costs” as required by 2 CFR 200.516(a)(3). To ensure a representative sample, we stratified the population by dollar amount (if applicable).

Because this finding reports non-compliance with State law, the Office of Financial Management is required by RCW 43.09.312 (1) to submit the agency’s response and plan for remediation to the Governor, the Joint Legislative Audit and Review Committee, and the relevant fiscal and policy committees of the Senate and House of Representatives.

Recommendations

We recommend the Department:

- Ensure proficiency improvement plans are reviewed thoroughly before approval
- Ensure that all providers’ background checks and Character, Competence and Suitability reviews are completed as required by State law and rule
- Identify all associated costs related to the unallowable payments for personal care services
- Consult with the U.S. Department of Health and Human Services to discuss whether the questioned costs identified in the audit should be repaid

Department’s Response

The Department partially concurs with this finding.

The Department concurs that there were five instances when a fingerprint background check was not performed within the required timeframe. In all cases, fingerprint background checks were completed and no disqualifying crimes were found.

The Department also concurs that there was one instance where a background check was not renewed after two years, which is a Department policy. However, the Medicaid State Plan for Community First Choice (CFC) does not require Individual Providers to complete background checks every two years

to remain qualified. The State Plan requires Individual Providers to complete a state background check prior to contracting, and a federal background check, when required, within 120 days of being hired.

The Department does not concur with the statement that the Department does not have adequate internal controls to ensure all Medicaid CFC individual providers (IPs) had proper background checks. Centers for Medicare and Medicaid Services requires a minimum of 86% proficiency related to compliance with IP background checks. The Department has monitored this requirement for many years and proficiency has always been over 90%. The Department will continue to follow established internal controls to materially ensure Community First Choice individual providers have timely background checks.

The Department does agree that two of the three Area Agency on Aging (AAA) proficiency improvement plans reviewed by the SAO did not address how the AAA would correct a background check deficiency. The Department will revise its internal process for approving proficiency improvement plans for accuracy and completeness to ensure all identified issues are addressed.

The Department will identify associated costs related to unallowable payments for personal care services. The Department will then work with the U.S. Department of Health and Human Services to return questioned costs.

Auditor's Concluding Remarks

While the Centers for Medicare and Medicaid Services require a minimum of 86 percent proficiency related to compliance with IP background checks, we determine a material weakness exists when an agency's key internal controls fail five percent or more of the time. Our audit testing showed the internal control related to IP background checks failed more than five percent of the time.

We reaffirm our finding and will review the status of the Department's corrective action during our next audit.

Applicable Laws and Regulations

Title 2 U.S. Code of Federal Regulations Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance) establishes the following applicable requirements:

Section 200.53 Improper Payments states:

- (a) *Improper payment* means any payment that should not have been made or that was made in an incorrect amount (including overpayments and underpayments) under statutory, contractual, administrative, or other legally applicable requirements; and
- (b) *Improper payment* includes any payment to an ineligible party, any payment for an ineligible good or service, any duplicate payment, any payment for a good or service not received (except for such payments where authorized by law), any payment that does not account for credit for applicable discounts, and any payment where insufficient or lack of documentation prevents a reviewer from discerning whether a payment was proper.

Section 200.303 Internal controls, states in part:

The non-Federal entity must:

- (a) Establish and maintain effective internal control over the Federal award that provides reasonable assurance that the non-Federal entity is managing the Federal award in compliance with Federal statutes, regulations, and the terms and conditions of the Federal award. These internal controls should be in compliance with guidance in “Standards for Internal Control in the Federal Government” issued by the Comptroller General of the United States or the “Internal Control Integrated Framework”, issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).
- (d) Take prompt action when instances of noncompliance are identified including noncompliance identified in audit findings.

Section 200.403 Factors affecting Allowability of costs.

Except where otherwise authorized by statute, costs must meet the following general criteria in order to be allowable under Federal awards.

- (a) Be necessary and reasonable for the performance of the Federal award and be allocable thereto under these principles.
- (b) Conform to any limitations or exclusions set forth in these principles or in the Federal award as to types or amount of cost items.
- (c) Be consistent with policies and procedures that apply uniformly to both federally-financed and other activities of the non-Federal entity.
- (d) Be accorded consistent treatment. A cost may not be assigned to a Federal award as a direct cost if any other cost incurred for the same purpose in like circumstances has been allocated to the Federal award as an indirect cost.
- (e) Be determined in accordance with generally accepted accounting principles (GAAP), except, for state and local governments and Indian tribes only, as otherwise provided for in this part.
- (f) Not be included as a cost or used to meet cost sharing or matching requirements of any other federally-financed program in either the current or a prior period. See also §200.306 Cost sharing or matching paragraph (b).
- (g) Be adequately documented. See also §§200.300 Statutory and national policy requirements through 200.309 Period of performance of this part.

Section 200.410 Collection of unallowable costs.

Payments made for costs determined to be unallowable by either the Federal awarding agency, cognizant agency for indirect costs, or pass-through entity, either as direct or indirect costs, must be refunded (including interest) to the Federal Government in accordance with instructions from the Federal agency that determined the costs are unallowable unless Federal statute or regulation directs otherwise. See also Subpart D— Post Federal Award Requirements of this part, §§200.300 Statutory and national policy requirements through 200.309 Period of performance.

Section 200.516 Audit findings, states in part:

- (a) *Audit findings reported.* The auditor must report the following as audit findings in a schedule of findings and questioned costs:

- (1) Significant deficiencies and material weaknesses in internal control over major programs and significant instances of abuse relating to major programs. The auditor's determination of whether a deficiency in internal control is a significant deficiency or material weakness for the purpose of reporting an audit finding is in relation to a type of compliance requirement for a major program identified in the Compliance Supplement.
- (3) Known questioned costs that are greater than \$25,000 for a type of compliance requirement for a major program. Known questioned costs are those specifically identified by the auditor. In evaluating the effect of questioned costs on the opinion on compliance, the auditor considers the best estimate of total costs questioned (likely questioned costs), not just the questioned costs specifically identified (known questioned costs). The auditor must also report known questioned costs when likely questioned costs are greater than \$25,000 for a type of compliance requirement for a major program. In reporting questioned costs, the auditor must include information to provide proper perspective for judging the prevalence and consequences of the questioned costs.

The American Institute of Certified Public Accountants defines significant deficiencies and material weaknesses in internal controls over compliance in its *Codification of Statements on Auditing Standards*, section 935, Compliance Audits, as follows:

.11 For purposes of adapting GAAS to a compliance audit, the following terms have the meanings attributed as follows: ...

Deficiency in internal control over compliance. A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance on a timely basis. A deficiency in design exists when (a) a control necessary to meet the control objective is missing, or (b) an existing control is not properly designed so that, even if the control operates as designed, the control objective would not be met. A deficiency in operation exists when a properly designed control does not operate as designed or the person performing the control does not possess the necessary authority or competence to perform the control effectively.

Material weakness in internal control over compliance. A deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a compliance requirement will not be prevented, or detected and corrected, on a timely basis. In this section, a reasonable possibility exists when the likelihood of an event occurring is either reasonably possible or probable as defined as follows:

Reasonably possible. The chance of the future event or events occurring is more than remote but less than likely.

Probable. The future event or events are likely to occur.

Significant deficiency in internal control over compliance. A deficiency, or a combination of deficiencies, in internal control over compliance that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

Office of Management and Budget OMB Uniform Guidance, Compliance Supplement for 2017, *Part 4 – Agency Program Requirements, 4.93.778 Medicaid Cluster*, states in part:

General Audit Approach for Medicaid Payments

To be allowable, Medicaid costs for medical services must be (1) covered by the State plan and waivers; (2) reviewed by the State consistent with the State’s documented procedures and system for determining medical necessity of claims; (3) properly coded; and (4) paid at the rate allowed by the State plan. Additionally, Medicaid costs must be net of beneficiary cost-sharing obligations and applicable credits (e.g., insurance, recoveries from other third parties who are responsible for covering the Medicaid costs, and drug rebates), paid to eligible providers, and only provided on behalf of eligible individuals.

Revised Code of Washington RCW 43.43.837, “Fingerprint-based background checks—Requirements for applicants and service providers—Shared background checks—Fees—Rules to establish financial responsibility,” states in part:

- (1) Except as provided in subsection (2) of this section, in order to determine the character, competence, and suitability of any applicant or service provider to have unsupervised access, the secretary may require a fingerprint-based background check through both the Washington state patrol and the federal bureau of investigation at any time, but shall require a fingerprint-based background check when the applicant or service provider has resided in the state less than three consecutive years before application, and:
 - (a) Is an applicant or service provider providing services to children or people with developmental disabilities under RCW [74.15.030](#);
 - (b) Is an individual residing in an applicant or service provider's home, facility, entity, agency, or business or who is authorized by the department to provide services to children or people with developmental disabilities under RCW [74.15.030](#); or
 - (c) Is an applicant or service provider providing in-home services funded by:
 - (i) Medicaid personal care under RCW [74.09.520](#);
 - (ii) Community options program entry system waiver services under RCW [74.39A.030](#);
 - (iii) Chore services under RCW [74.39A.110](#); or
 - (iv) Other home and community long-term care programs, established pursuant to chapters [74.39](#) and [74.39A](#) RCW, administered by the department.
- (2) Long-term care workers, as defined in RCW [74.39A.009](#), who are hired after January 7, 2012, are subject to background checks under RCW [74.39A.056](#).
- (3) To satisfy the shared background check requirements provided for in RCW [43.215.215](#) and [43.20A.710](#), the department of early learning and the department of social and health services shall share federal fingerprint-based background check results as permitted under the law. The purpose of this provision is to allow both departments to fulfill their joint background check responsibility of checking any individual who may have unsupervised access to vulnerable adults, children, or juveniles. Neither department may share the federal background check results with any other state agency or person.

- (4) The secretary shall require a fingerprint-based background check through the Washington state patrol identification and criminal history section and the federal bureau of investigation when the department seeks to approve an applicant or service provider for a foster or adoptive placement of children in accordance with federal and state law.
- (5) Any secure facility operated by the department under chapter [71.09](#) RCW shall require applicants and service providers to undergo a fingerprint-based background check through the Washington state patrol identification and criminal history section and the federal bureau of investigation.
- (6) Service providers and service provider applicants who are required to complete a fingerprint-based background check may be hired for a one hundred twenty-day provisional period as allowed under law or program rules when:
 - (a) A fingerprint-based background check is pending; and
 - (b) The applicant or service provider is not disqualified based on the immediate result of the background check.
- (7) Fees charged by the Washington state patrol and the federal bureau of investigation for fingerprint-based background checks shall be paid by the department for applicants or service providers providing:
 - (a) Services to people with a developmental disability under RCW [74.15.030](#);
 - (b) In-home services funded by medicaid personal care under RCW [74.09.520](#);
 - (c) Community options program entry system waiver services under RCW [74.39A.030](#);
 - (d) Chore services under RCW [74.39A.110](#);
 - (e) Services under other home and community long-term care programs, established pursuant to chapters [74.39](#) and [74.39A](#) RCW, administered by the department;
 - (f) Services in, or to residents of, a secure facility under RCW [71.09.115](#); and
 - (g) Foster care as required under RCW [74.15.030](#).
- (8) Service providers licensed under RCW [74.15.030](#) must pay fees charged by the Washington state patrol and the federal bureau of investigation for conducting fingerprint-based background checks.
- (9) Children's administration service providers licensed under RCW [74.15.030](#) may not pass on the cost of the background check fees to their applicants unless the individual is determined to be disqualified due to the background information.
- (10) The department shall develop rules identifying the financial responsibility of service providers, applicants, and the department for paying the fees charged by law enforcement to roll, print, or scan fingerprints-based for the purpose of a Washington state patrol or federal bureau of investigation fingerprint-based background check.
- (11) For purposes of this section, unless the context plainly indicates otherwise:
 - (a) Applicant" means a current or prospective department or service provider employee, volunteer, student, intern, researcher, contractor, or any other individual who will or may have unsupervised access because of the nature of the work or services he or she provides. "Applicant" includes but is not limited to any individual who will or may have unsupervised access and is:
 - (i) Applying for a license or certification from the department;
 - (ii) Seeking a contract with the department or a service provider;
 - (iii) Applying for employment, promotion, reallocation, or transfer;
 - (iv) An individual that a department client or guardian of a department client chooses to hire or engage to provide services to himself or herself or another vulnerable

adult, juvenile, or child and who might be eligible to receive payment from the department for services rendered; or

- (v) A department applicant who will or may work in a department-covered position.
- (b) "Authorized" means the department grants an applicant, home, or facility permission to:
 - (i) Conduct licensing, certification, or contracting activities;
 - (ii) Have unsupervised access to vulnerable adults, juveniles, and children;
 - (iii) Receive payments from a department program; or
 - (iv) Work or serve in a department-covered position.
- (c) "Department" means the department of social and health services.
- (d) "Secretary" means the secretary of the department of social and health services.
- (e) "Secure facility" has the meaning provided in RCW [71.09.020](#).
- (f) "Service provider" means entities, facilities, agencies, businesses, or individuals who are licensed, certified, authorized, or regulated by, receive payment from, or have contracts or agreements with the department to provide services to vulnerable adults, juveniles, or children. "Service provider" includes individuals whom a department client or guardian of a department client may choose to hire or engage to provide services to himself or herself or another vulnerable adult, juvenile, or child and who might be eligible to receive payment from the department for services rendered. "Service provider" does not include those certified under *chapter [70.96A](#) RCW.

Revised Code of Washington 74.15.030, Powers and duties of secretary, states:

The secretary shall have the power and it shall be the secretary's duty:

- (1) In consultation with the children's services advisory committee, and with the advice and assistance of persons representative of the various type agencies to be licensed, to designate categories of facilities for which separate or different requirements shall be developed as may be appropriate whether because of variations in the ages, sex and other characteristics of persons served, variations in the purposes and services offered or size or structure of the agencies to be licensed hereunder, or because of any other factor relevant thereto;
- (2) In consultation with the children's services advisory committee, and with the advice and assistance of persons representative of the various type agencies to be licensed, to adopt and publish minimum requirements for licensing applicable to each of the various categories of agencies to be licensed.

The minimum requirements shall be limited to:

- (a) The size and suitability of a facility and the plan of operation for carrying out the purpose for which an applicant seeks a license;
- (b) Obtaining background information and any out-of-state equivalent, to determine whether the applicant or service provider is disqualified and to determine the character, competence, and suitability of an agency, the agency's employees, volunteers, and other persons associated with an agency;
- (c) Conducting background checks for those who will or may have unsupervised access to children, expectant mothers, or individuals with a developmental disability; however, a background check is not required if a caregiver approves an activity pursuant to the prudent parent standard contained in RCW [74.13.710](#);

- (d) Obtaining child protective services information or records maintained in the department case management information system. No unfounded allegation of child abuse or neglect as defined in RCW [26.44.020](#) may be disclosed to a child-placing agency, private adoption agency, or any other provider licensed under this chapter;
 - (e) Submitting a fingerprint-based background check through the Washington state patrol under chapter [10.97](#) RCW and through the federal bureau of investigation for:
 - (i) Agencies and their staff, volunteers, students, and interns when the agency is seeking license or relicense;
 - (ii) Foster care and adoption placements; and
 - (iii) Any adult living in a home where a child may be placed;
 - (f) If any adult living in the home has not resided in the state of Washington for the preceding five years, the department shall review any child abuse and neglect registries maintained by any state where the adult has resided over the preceding five years;
 - (g) The cost of fingerprint background check fees will be paid as required in RCW [43.43.837](#);
 - (h) National and state background information must be used solely for the purpose of determining eligibility for a license and for determining the character, suitability, and competence of those persons or agencies, excluding parents, not required to be licensed who are authorized to care for children or expectant mothers;
 - (i) The number of qualified persons required to render the type of care and treatment for which an agency seeks a license;
 - (j) The safety, cleanliness, and general adequacy of the premises to provide for the comfort, care and well-being of children, expectant mothers or developmentally disabled persons;
 - (k) The provision of necessary care, including food, clothing, supervision and discipline; physical, mental and social well-being; and educational, recreational and spiritual opportunities for those served;
 - (l) The financial ability of an agency to comply with minimum requirements established pursuant to chapter [74.15](#) RCW and RCW [74.13.031](#); and
 - (m) The maintenance of records pertaining to the admission, progress, health and discharge of persons served;
- (3) To investigate any person, including relatives by blood or marriage except for parents, for character, suitability, and competence in the care and treatment of children, expectant mothers, and developmentally disabled persons prior to authorizing that person to care for children, expectant mothers, and developmentally disabled persons. However, if a child is placed with a relative under RCW [13.34.065](#) or [13.34.130](#), and if such relative appears otherwise suitable and competent to provide care and treatment the criminal history background check required by this section need not be completed before placement, but shall be completed as soon as possible after placement;
- (4) On reports of alleged child abuse and neglect, to investigate agencies in accordance with chapter [26.44](#) RCW, including child day-care centers and family day-care homes, to determine whether the alleged abuse or neglect has occurred, and whether child protective services or referral to a law enforcement agency is appropriate;

- (5) To issue, revoke, or deny licenses to agencies pursuant to chapter [74.15](#) RCW and RCW [74.13.031](#). Licenses shall specify the category of care which an agency is authorized to render and the ages, sex and number of persons to be served;
- (6) To prescribe the procedures and the form and contents of reports necessary for the administration of chapter [74.15](#) RCW and RCW [74.13.031](#) and to require regular reports from each licensee;
- (7) To inspect agencies periodically to determine whether or not there is compliance with chapter [74.15](#) RCW and RCW [74.13.031](#) and the requirements adopted hereunder;
- (8) To review requirements adopted hereunder at least every two years and to adopt appropriate changes after consultation with affected groups for child day-care requirements and with the children's services advisory committee for requirements for other agencies; and
- (9) To consult with public and private agencies in order to help them improve their methods and facilities for the care of children, expectant mothers and developmentally disabled persons.

Washington Administrative Code 388-71-0510 – “How does a person become an individual provider?” states:

In order to become an individual provider, a person must:

- (1) Be eighteen years of age or older;
- (2) Provide the social worker/case manager/designee with:
 - (a) A valid Washington state driver's license or other valid picture identification; and either
 - (b) A Social Security card; or
 - (c) Proof of authorization to work in the United States.
- (3) Complete the required DSHS form authorizing a background check;
- (4) Disclose any criminal convictions and pending charges, and also disclose civil adjudication proceedings and negative actions as those terms are defined in WAC 388-71-0512;
- (5) Effective January 8, 2012, be screened through Washington state's name and date of birth background check. Preliminary results may require a thumb print for identification purposes.
- (6) Effective January 8, 2012, be screened through the Washington state and national fingerprint-based background check, as required by RCW 74.39A.056.
- (7) Results of background checks are provided to the department and the employer or potential employer unless otherwise prohibited by law or regulation for the purpose of determining whether the person:
 - (a) Is disqualified based on a disqualifying criminal conviction or a pending charge for a disqualifying crime as listed in WAC 388-113-0020, civil adjudication proceeding, or negative action as defined in WAC 388-71-0512 and 388-71-0540; or
 - (b) Should or should not be employed as an individual provider based on his or her character, competence, and/or suitability.
- (8) For those providers listed in RCW 43.43.837(1), a second Washington state and national fingerprint-based background check is required if they have lived out of the state of Washington since the first national fingerprint-based background check was completed.

(9) The department may require an individual provider to have a Washington state name and date of birth background check or a Washington state and national fingerprint-based background check, or both, at any time.

(10) Sign a home and community-based service provider contract/agreement to provide personal care services to a person under a medicaid state plan or federal waiver such as COPES or other waiver programs.

2018-057 **The Department of Social and Health Services, Aging and Long-Term Support and Developmental Disabilities Administrations, did not have adequate internal controls over and did not comply with requirements to ensure some Medicaid providers were properly revalidated or screened, and fingerprint-based criminal background check requirements were met.**

Federal Awarding Agency: U.S. Department of Health and Human Services
Pass-Through Entity: None
CFDA Number and Title: 93.775 State Medicaid Fraud Control Units
93.777 State Survey and Certification of Health Care Providers and Suppliers (Title XVIII) Medicare
93.778 Medical Assistance Program (Medicaid; Title XIX)
Federal Award Number: 1805WA5MAP; 1805WA5ADM; 1805WAIMPL; 1805WAINCT
Applicable Compliance Component: Special Tests and Provisions – Provider Eligibility-Provider Revalidation
Known Questioned Cost Amount: None

Background

Medicaid is a jointly funded state and federal partnership providing coverage for about 1.9 million eligible low-income Washington residents who otherwise might go without medical care. Medicaid is Washington’s largest public assistance program and accounts for about one-third of the State’s federal expenditures. The program spent about \$12.7 billion in federal and state funds during fiscal year 2018.

Provider enrollment

In March 2011, a new federal regulation required state Medicaid agencies to revalidate the enrollment of all Medicaid providers at least every five years. The Centers for Medicare and Medicaid Services (CMS) notified states through an informational bulletin that the revalidation of all providers enrolled on or before March 25, 2011, must be completed by March 24, 2016.

In January 2016, CMS issued updated guidance to states that extended the deadline for provider revalidation to September 25, 2016. The new deadline applied to all providers enrolled on or before September 25, 2011. After this deadline, all providers must be revalidated every five years from their initial enrollment date. As part of this updated guidance, CMS required states to notify all affected providers of the revalidation requirement by the original March 24, 2016, deadline.

The Department of Social and Health Services (Department) revalidates the enrollment of Medicaid providers through its contracting process. Individual provider contract terms are four years and contracting requirements are screened by a contract specialist within the Department’s Aging and Long-

Term Support (ALTSA) and Developmental Disabilities (DDA) Administrations. Contracts are also screened by Area Agencies on Aging (AAA) regional offices. A valid Washington state driver's license or other valid picture identification and either a Social Security card or proof of authorization to work in the United States must be checked during revalidation for individual providers. Nursing facility contract expiration dates are open ended, but the contract unit revalidates nursing facility enrollment every five years; contracting requirements are screened by the Department's contract unit.

Federal law requires the State Medicaid agency to check the following during its revalidation process:

- Social Security Administration's Death Master File (DMF)
- National Plan and Provider Enumeration System (NPPES)
- List of Excluded Individuals/Entities (LEIE)
- Excluded Parties List System (EPLS) (now known as the System for Award Management (SAM))

The Department's contract unit performs daily federal database checks for all providers. When a provider's contract is revalidated, a contract file is created in the Agency Contracts Database (ACD). The results are documented in the "Check" section of the ACD system. Before signing a contract, a contract specialist checks the ACD system to ensure the federal database checks were performed and properly documented.

Provider screening risk levels

The first step in revalidating a provider is to determine the provider's screening risk level. A provider can be designated as one of three risk levels: limited, moderate or high. Each risk level requires progressively greater scrutiny of the provider before it can be revalidated. CMS issued initial guidance on screening levels for specific provider types. For providers enrolled in both Medicare and Medicaid, state Medicaid agencies must assign providers to the same or higher risk category applicable under Medicare. In addition, certain provider behaviors require a provider to be moved to a higher screening risk level.

The following are the required screening procedures for each of the risk levels:

Limited risk

- Verify that provider meets applicable federal regulations or state requirements for provider type before making an enrollment determination
- Conduct license verifications, including for licenses in states other than where the provider is enrolling
- Conduct database checks to ensure providers continue to meet the enrollment criteria for their provider type

Moderate risk

- Perform the "limited" screening requirements
- Conduct onsite visits

High risk

- Perform the “limited” and “moderate” screening requirements
- Conduct a fingerprint-based criminal background check

State Medicaid agencies must adjust the categorical risk level of a particular provider from “limited” or “moderate” to “high” when any of the following situations occur:

- A Medicaid agency imposes a payment suspension on a provider based on credible allegation of fraud, waste or abuse. The provider’s risk remains “high” for 10 years after the date the payment suspension was issued.
- A provider that, upon applying for enrollment or revalidation, is found to have an existing state Medicaid Plan overpayment which is \$1,500 or greater and more than 30 days old.
- The provider has been excluded by the Office of Inspector General or another state’s Medicaid program in the previous 10 years.
- A Medicaid agency or CMS, in the previous six months, lifted a temporary moratorium for the particular provider type and a provider that was prevented from enrolling based on the moratorium applies for enrollment as a provider at any time within six months from the date the moratorium was lifted

Fingerprint-based criminal background check

In revalidating a provider’s enrollment, the state Medicaid agency must conduct a fingerprint-based criminal background check when the agency has designated a provider as high-risk. Anyone with at least a 5 percent direct or indirect ownership interest in a business that provides Medicaid services is also subject to the fingerprint check requirement. The deadline to fully-implement a fingerprint-based criminal background check process was June 1, 2016, and the State Medicaid agency was required to ensure it had processes in place to complete the following tasks related to fingerprint-based criminal background checks:

- Notify each provider in the high risk category about the fingerprint-based criminal background check requirement
- Collect and use fingerprints to verify whether the provider or any person with a 5 percent or more or indirect ownership interest in the provider has a criminal history in the state or, if it chooses, at the national level
- Take any necessary termination action based on the criminal history data and updated enrollment records to reflect fingerprint-based criminal background check status
- Indicate in the enrollment record for a provider in the high-risk category whether and when the provider passed, failed or failed to respond to the requirement for fingerprint-based criminal background checks

On August 1, 2017, CMS extended the deadline to implement a fingerprint-based criminal background check process to July 1, 2018.

The Department paid Medicaid providers about \$2.8 billion for fee-for-service claims in fiscal year 2018. The two highest paid provider types were individual providers and nursing facilities. In fiscal

year 2018, the Department paid about \$662 million to more than 45,000 individual providers and about \$644 million to 256 nursing facilities.

Description of Condition

The Department did not have adequate internal controls over and did not comply with requirements to ensure Medicaid providers were revalidated every five years or that screening and fingerprint-based criminal background check requirements were met.

Provider enrollment

We found the Department did not ensure federally required database checks were performed before completing enrollment revalidation of individual providers and nursing facilities.

We also found that the Department did not ensure all nursing facilities were revalidated by the deadline. The Department began revalidating nursing facilities in November 2017.

Provider screening levels

The Department did not establish a process to adjust provider screening risk levels during the period.

Fingerprint-based criminal background check

The Department did not implement a fingerprint-based criminal background check process for all providers categorized as high risk by the extended deadline of July 1, 2018.

We consider these internal control deficiencies to be a material weakness.

This condition was not reported in the prior audit.

Cause of Condition

DMF checks were not consistently performed until the Department implemented a daily check process in November 2016. The Department was not aware that NPPES checks for nursing facilities should be performed when a nursing facility was revalidated.

The Department did not implement the risk adjustment process and a fingerprint-based criminal background check for high-risk providers during our audit period and revalidation for nursing facilities until November 2017 because it was not aware of the new revalidation rules.

Effect of Condition

Using a statistical sampling method, we randomly selected 86 individual providers that were paid by AL TSA during the audit period from a population of 32,860 providers. We identified a total of 102 contracts associated with the payments made to the 86 providers.

Additionally, we randomly selected 86 individual providers that were paid by DDA during the audit period from a population of 14,494 providers. We identified a total of 99 contracts associated with the payments made for the 86 DDA providers.

We also randomly selected 53 nursing facilities that were paid during the audit period from a population of 256 facilities. We identified 53 contracts associated with the payments made for the 53 facilities.

We reviewed the selected contracts to determine if the Department took proper steps when conducting provider revalidations. We found:

- Database checks were not completed for 64 AL TSA individual provider contracts
- Database checks were not completed for 68 DDA individual provider contracts
- Database checks were not completed for 36 nursing facility contracts
- 36 nursing facilities were not revalidated by the deadline

Provider Type	LEIE check not properly completed	EPLS check not properly completed	DMF check not properly completed	NPPES check not properly completed	Contracts signed before federal database checks	Totals
AL TSA providers	6	6	57	N/A ¹	29	64 ²
DDA providers	1	1	67	N/A ¹	7	68 ²
Nursing facilities	0	0	8	36	0	36 ²

- 1.NPPES check is not required for individual providers because National Provider Identifier (NPI) is not required for individual providers.
- 2.Some contracts had multiple issues.

We also reviewed Department records to determine if it obtained proof of authorization to work in the U.S. and a copy of picture identification cards from individual providers before revalidating their contracts.

We found:

- One instance when DDA records did not contain evidence showing an individual provider was authorized to work in the U.S.
- Five instances when AL TSA records did not contain evidence showing individual providers had valid picture identification
- Five instances when DDA records did not contain evidence showing individual providers had valid picture identification

By not complying with provider revalidation, screening and fingerprint-based criminal background check requirements, the Department faces a higher risk of not detecting when Medicaid providers are ineligible to provide services or be paid with Medicaid funds.

Recommendations

We recommend the Department:

- Implement adequate internal controls to ensure provider revalidations are properly completed by established deadlines
- Ensure federal database checks are completed at the time of provider revalidation
- Verify and properly document that individual providers are authorized to work in the U.S. and have a valid picture identification card at the time of revalidation
- Implement a process to adjust providers' screening risk levels
- Implement a process to conduct fingerprint-based criminal background checks for high-risk providers

Department's Response

The Department concurs with this finding.

In November 2017, the Department developed a process to screen and track each nursing facility contract to ensure validation and revalidation occurs within the five-year requirement. It was not until September of 2018 that the nursing facility screenings were completed due to delayed response, and the return of required forms, by the nursing facilities. Currently, all nursing facilities have been screened as required.

Effective October 8, 2018, the Department implemented the new Automated Provider Screening process in the Agency Contracts Database (ACD). The new process includes an internal control that prevents a new or renewal Medicaid contract to be approved or signed unless the screening process has been successfully completed in ACD.

The Provider Risk Level reassignment, due to overpayment or Medicaid fraud referral, is under Department review to determine workload impact and costs associated with adding monitoring of risk levels to on-going contracting efforts. Once workload impact and cost analysis is complete, the Department will determine the best course of action to comply with screening and fingerprint requirements.

Auditor's Concluding Remarks

We thank the Department for its cooperation and assistance throughout the audit. We will review the status of the Department's corrective action during our next audit.

Applicable Laws and Regulations

Title 2 U.S. Code of Federal Regulations Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance) establishes the following applicable requirements:

Section 200.303 Internal controls.

The non-Federal entity must:

- (a) Establish and maintain effective internal control over the Federal award that provides reasonable assurance that the non-Federal entity is managing the Federal award in compliance with Federal statutes, regulations, and the terms and conditions of the Federal award. These internal controls should be in compliance with guidance in “Standards for Internal Control in the Federal Government” issued by the Comptroller General of the United States or the “Internal Control Integrated Framework”, issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).
- (b) Comply with Federal statutes, regulations, and the terms and conditions of the Federal awards.
- (d) Take prompt action when instances of noncompliance are identified including noncompliance identified in audit findings.

Section 200.516 Audit findings, states in part:

- (a) *Audit findings reported.* The auditor must report the following as audit findings in a schedule of findings and questioned costs:
 - (1) Significant deficiencies and material weaknesses in internal control over major programs and significant instances of abuse relating to major programs. The auditor’s determination of whether a deficiency in internal control is a significant deficiency or material weakness for the purpose of reporting an audit finding is in relation to a type of compliance requirement for a major program identified in the Compliance Supplement.
 - (2) Material noncompliance with the provisions of Federal statutes, regulations, or the terms and conditions of Federal awards related to a major program. The auditor’s determination of whether a noncompliance with the provisions of Federal statutes, regulations, or the terms and conditions of Federal awards is material for the purpose of reporting an audit finding is in relation to a type of compliance requirement for a major program identified in the compliance supplement.

The American Institute of Certified Public Accountants defines significant deficiencies and material weaknesses in internal controls over compliance in its *Codification of Statements on Auditing Standards*, section 935, Compliance Audits, as follows:

.11 For purposes of adapting GAAS to a compliance audit, the following terms have the meanings attributed as follows: ...

Deficiency in internal control over compliance. A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance on a timely basis. A deficiency in design

exists when (a) a control necessary to meet the control objective is missing, or (b) an existing control is not properly designed so that, even if the control operates as designed, the control objective would not be met. A deficiency in operation exists when a properly designed control does not operate as designed or the person performing the control does not possess the necessary authority or competence to perform the control effectively.

Material weakness in internal control over compliance. A deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a compliance requirement will not be prevented, or detected and corrected, on a timely basis. In this section, a reasonable possibility exists when the likelihood of an event occurring is either reasonably possible or probable as defined as follows:

Reasonably possible. The chance of the future event or events occurring is more than remote but less than likely.

Probable. The future event or events are likely to occur.

Significant deficiency in internal control over compliance. A deficiency, or a combination of deficiencies, in internal control over compliance that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

Material noncompliance. In the absence of a definition of material noncompliance in the governmental audit requirement, a failure to follow compliance requirements or a violation of prohibitions included in the applicable compliance requirements that results in noncompliance that is quantitatively or qualitatively material, either individually or when aggregated with other noncompliance, to the affected government program.

Title 42 U.S. Code of Federal Regulations section 455 Subpart E – Provider Screening and Enrollment, states in part:

Section 455.414 Revalidation of enrollment

The State Medicaid agency must revalidate the enrollment of all providers regardless of provider type at least every 5 years.

Section 455.434 Criminal background checks

The State Medicaid agency -

- (a) As a condition of enrollment, must require providers to consent to criminal background checks including fingerprinting when required to do so under State law or by the level of screening based on risk of fraud, waste or abuse as determined for that category of provider.
- (b) Must establish categorical risk levels for providers and provider categories who pose an increased financial risk of fraud, waste or abuse to the Medicaid program.
 - (1) Upon the State Medicaid agency determining that a provider, or a person with a 5 percent or more direct or indirect ownership interest in the provider, meets the State Medicaid agency's criteria hereunder for criminal background checks as a “high” risk to the Medicaid program, the State Medicaid agency will require that each such provider or person submit fingerprints.
 - (2) The State Medicaid agency must require a provider, or any person with a 5 percent or more direct or indirect ownership interest in the provider, to submit a

set of fingerprints, in a form and manner to be determined by the State Medicaid agency, within 30 days upon request from CMS or the State Medicaid agency.

Section 455.450 Screening levels for Medicaid providers.

A State Medicaid agency must screen all initial applications, including applications for a new practice location, and any applications received in response to a re-enrollment or revalidation of enrollment request based on a categorical risk level of “limited,” “moderate,” or “high.” If a provider could fit within more than one risk level described in this section, the highest level of screening is applicable.

- (a) Screening for providers designated as limited categorical risk. When the State Medicaid agency designates a provider as a limited categorical risk, the State Medicaid agency must do all of the following:
 - (1) Verify that a provider meets any applicable Federal regulations, or State requirements for the provider type prior to making an enrollment determination.
 - (2) Conduct license verifications, including State licensure verifications in States other than where the provider is enrolling, in accordance with § 455.412.
 - (3) Conduct database checks on a pre- and post-enrollment basis to ensure that providers continue to meet the enrollment criteria for their provider type, in accordance with § 455.436.
- (b) Screening for providers designated as moderate categorical risk. When the State Medicaid agency designates a provider as a “moderate” categorical risk, a State Medicaid agency must do both of the following:
 - (1) Perform the “limited” screening requirements described in paragraph (a) of this section.
 - (2) Conduct on-site visits in accordance with § 455.432.
- (c) Screening for providers designated as high categorical risk. When the State Medicaid agency designates a provider as a “high” categorical risk, a State Medicaid agency must do both of the following:
 - (1) Perform the “limited” and “moderate” screening requirements described in paragraphs (a) and (b) of this section.
 - (2) (i) Conduct a criminal background check; and (ii) Require the submission of a set of fingerprints in accordance with § 455.434.
- (d) Denial or termination of enrollment. A provider, or any person with 5 percent or greater direct or indirect ownership in the provider, who is required by the State Medicaid agency or CMS to submit a set of fingerprints and fails to do so may have its -
 - (1) Application denied under § 455.434; or
 - (2) Enrollment terminated under § 455.416.
- (e) Adjustment of risk level. The State agency must adjust the categorical risk level from “limited” or “moderate” to “high” when any of the following occurs:
 - (1) The State Medicaid agency imposes a payment suspension on a provider based on credible allegation of fraud, waste or abuse, the provider has an existing Medicaid overpayment, or the provider has been excluded by the OIG or another State's Medicaid program within the previous 10 years.
 - (2) The State Medicaid agency or CMS in the previous 6 months lifted a temporary moratorium for the particular provider type and a provider that was prevented

from enrolling based on the moratorium applies for enrollment as a provider at any time within 6 months from the date the moratorium was lifted.

Section 455.436 Federal database checks.

The State Medicaid agency must do all of the following:

- (a) Confirm the identity and determine the exclusion status of providers and any person with an ownership or control interest or who is an agent or managing employee of the provider through routine checks of Federal databases.
- (b) Check the Social Security Administration's Death Master File, the National Plan and Provider Enumeration System (NPPES), the List of Excluded Individuals/Entities (LEIE), the Excluded Parties List System (EPLS), and any such other databases as the Secretary may prescribe.

Centers for Medicare and Medicaid Services, Center for Medicaid and CHIP Services, CMCS Informational Bulletin, dated December 21, 2011, states in part:

The Federal regulation at 42 CFR 455.414 requires States, beginning March 25, 2011, to complete revalidation of enrollment for all providers, regardless of provider type, at least every five years. Based upon this requirement, States must complete the revalidation process of all provider types by March 24, 2016.

Centers for Medicare and Medicaid Services (CMS) Sub Regulatory Guidance for State Medicaid Agencies (SMA): Revalidation (2016-001) states in part:

The federal regulation at 42 CFR 455.414 requires that state Medicaid agencies revalidate the enrollment of all providers, regardless of provider types, at least every 5 years. The regulation was effective March 25, 2011. Based on this requirement, in a December 23, 2011 CMCS Informational Bulletin, we directed states to complete the revalidation process of all provider types by March 24, 2016.

The purpose of this guidance is to revise previous guidance in order to align Medicare and Medicaid revalidation activities to the greatest extent possible. We are revising that previous guidance to now require a two-step deadline under which states must notify all affected providers of the revalidation requirement by the original March 24, 2016 deadline, and must have completed the revalidation process by a new deadline of September 25, 2016.

...

- (3) Deadline for SMA to revalidate providers enrolled on or before September 25, 2011. The Federal regulation at 42 CFR § 455.414 requires states, beginning March 25, 2011, to revalidate the enrollment of all Medicaid providers, regardless of provider type, at least every five years. Based upon this requirement, by March 24, 2016, states must notify providers that were enrolled on or before March 25, 2011 that they must revalidate their enrollment. On March 25, 2016, states that have notified all providers subject to the revalidation requirement will be considered compliant with the revalidation activities required as of that date.

Washington Administrative Code 388-71-0510

How does a person become an individual provider?

In order to become an individual provider, a person must:

- (1) Be eighteen years of age or older;
- (2) Provide the social worker/case manager/designee with:
 - (a) A valid Washington state driver's license or other valid picture identification;
and either
 - (b) A Social Security card; or
 - (c) Proof of authorization to work in the United States.

2018-058

The Department of Social and Health Services, Developmental Disabilities Administration, did not have adequate internal controls over and was not compliant with requirements to ensure Medicaid payments to supported living providers were allowable.

Federal Awarding Agency: U.S. Department of Health and Human Services
Pass-Through Entity: None
CFDA Number and Title: 93.775 State Medicaid Fraud Control Units
93.777 State Survey and Certification of Health Care Providers and Suppliers (Title XVIII) Medicare
93.778 Medical Assistance Program (Medicaid; Title XIX)
Federal Award Number: 1805WA5MAP; 1805WA5ADM; 1805WAIMPL; 1805WAINCT
Applicable Compliance Component: Activities Allowed / Unallowed Cost Principles
Known Questioned Cost Amount: \$1,985,968

Background

Medicaid is a jointly funded state and federal partnership providing coverage for about 1.9 million eligible low-income Washington residents who otherwise might go without medical care. Medicaid is Washington's largest public assistance program and accounts for about one-third of the State's federal expenditures. The program spent about \$12.7 billion in federal and state funds during fiscal year 2018.

The Department of Social and Health Services' (Department) Developmental Disabilities Administration administers the Home and Community Based Services (HCBS) program for people with developmental disabilities. HCBS is a waiver program that permits states to provide an array of community-based services to help Medicaid clients live in the community and avoid institutionalization. States have broad discretion to design waiver programs, but those programs must be approved by the Centers for Medicare and Medicaid Services (CMS).

Supported living services support Medicaid clients to live in their own homes with one to three other people and receive instruction and support delivered by contracted service agencies (providers). Supported living clients pay their own rent, food and other personal expenses. Supported living is an option under the Home and Community Based Services Core and Community Protection waivers. In fiscal year 2018, the state Medicaid program paid about \$458 million in federal and state funds to supported living agencies that provided care to about 4,200 Medicaid clients.

Client assessments

The Department uses an assessment to evaluate client support needs and to calculate the number of support hours a client needs to live in the community. The assessment predicts a level of support as if the client lives alone. However, because some support hours can be shared with housemates, the Department looks for such shared-hour opportunities to help providers support clients in a cost-effective manner.

Through a rate setting process, Department resource managers work with providers to determine how the assessed level of support will be delivered and the number of daily direct service hours that will be provided. State rule requires providers to obtain Department approval of schedules to provide 24-hour support when household configurations change or when additional staffing is requested or needed by a client. Once determined, a daily rate is loaded into the Department's payment system, and providers access the system to claim payment for each day of service that was provided.

Cost reports

Providers must prepare and submit a cost report at the end of each calendar year. The Department uses cost report information to:

- Provide program cost data to regional managers and residential providers;
- Provide information to establish rates or allocate appropriated funds;
- Determine settlements with supported living providers;
- Provide information to the Legislature and the Department for budget development and policy decisions; and
- Provide accountability and transparency for the use of public funds.

Cost reports consist of 16 different schedules of provider information. The Department has established a template, accompanied by detailed instructions, that all providers must use when preparing cost reports. Providers must attest to the accuracy of the reported information.

In its approved Core waiver, the Department states that cost reports are desk audited to determine accuracy and the reasonableness of reported costs. The Department has also established a policy that states it will analyze the cost reports and financial statements of each provider to determine if the submitted information is correct and complete, and that it conforms with generally accepted accounting principles and applicable policies rules and regulations.

Provider documentation requirements

According to Department policy, providers must maintain detailed payroll records, by employee, of the hours and costs reported on their cost reports. The Department may request job descriptions for employees to verify the duties of positions. Paid hours and payroll costs for direct hours to clients must be verifiable in provider records. This includes employee timesheets and schedules for actual hours worked. In its cost report instructions, the Department states the detailed payroll information does not need to be submitted with cost reports. The Department has established a template that providers can use to organize the information, but providers are allowed to use their own payroll records.

When a provider uses its own payroll records, the Department requires in its instructions that the information clearly show the distinction between direct and non-direct hours and wages for the provider's employees and that each employee be assigned to one of seven different job classification categories. The instructions further state that the detailed payroll records must be made available if requested by the Department for auditing purposes.

Settlements

After reviewing cost reports, the Department establishes settlements when providers were paid for more direct service hours than they provided in a calendar year (Settlement A) or when providers received more reimbursement (in dollars) for direct support costs compared with what was actually incurred during the year (Settlement B). Settlements are based on a provider's attestation of total hours provided or the total direct support dollars reimbursed, during the year. The Department's policy requires that providers refund the greater amount of Settlement A or B.

Once settlements are assessed, they are forwarded to the Department's collection arm, the Office of Financial Recovery (OFR), which records an overpayment and seeks repayment from providers.

Prior audit findings

In prior audits, we reported the Department did not have adequate internal controls over and was not compliant with requirements to ensure payments to supported living providers were allowable. The prior finding numbers were: 2017-044, 2016-041, 2016-045, 2015-049, 2015-052, 2014-041, 2014-042, 2013-036, 2013-038 and 12-39.

Description of Condition

The Department of Social and Health Services, Developmental Disabilities Administration, did not have adequate internal controls over and was not compliant with requirements to ensure Medicaid payments to supported living providers were allowable.

Cost reports and settlements

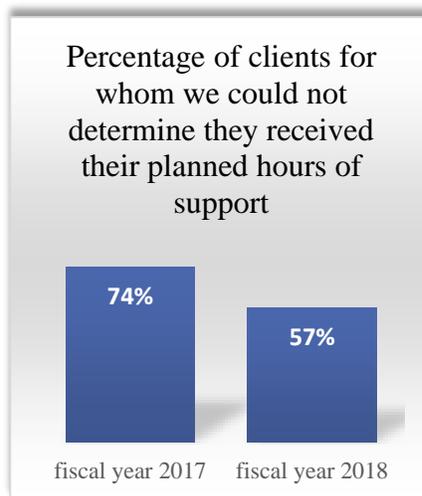
After obtaining cost reports from providers for the 2017 calendar year, the Department did not establish procedures to verify if the direct hours reported as worked, or the cost to provide those hours, were accurate and conformed with generally accepted accounting principles.

We used a statistically valid sampling method to randomly select 69 of the 123 cost reports the Department obtained from providers for the 2017 calendar year. We then independently requested payroll records from the providers to perform our own reconciliation. All providers responded to our request for records. In five instances (7 percent), the payroll records submitted by providers did not fully support the number of direct service hours that were reported on their cost reports. Additionally, in 43 instances (62 percent), providers did not properly categorize their employees as required by the Department's instructions.

In 35 instances (51 percent), providers were paid for more direct service hours than they reported on their cost reports. Before making this conclusion, we reviewed and considered the information the Department forwarded to OFR to be collected.

Employee timesheets

The Department pays providers for a client’s assessed level of support hours. We used a statistical sampling method to randomly select and examine 86 monthly payments from a population of 49,419 monthly payments made for client support hours. We requested employee timesheets and work schedules from providers for the selected months and reconciled employee direct support hours provided to clients to the hours the providers said they planned to provide to clients during the month. In 49 instances (57 percent), we could not determine that providers delivered a client’s planned level of hourly support.



Specifically, we identified 99,237 support hours that providers reported to the Department they planned to provide to clients based on their residential staffing plans. Of those hours, we verified providers delivered 89,119 support hours. For 10,118 hours (10 percent), we could not determine if the hours were provided because employees were not scheduled to work or supporting documentation was lacking.

For four of the households in our sample, totaling 4,600 planned hours of support, providers responded to our request for timesheets, but because of poor recordkeeping we could not determine if any hours of support were delivered to sampled clients.

We consider these control deficiencies to be a material weakness.

Duplicate payments

We tested to determine if the Department made duplicate payments to providers. We found the Department made 10 duplicate payments to providers, totaling \$4,082.

Cause of Condition

Cost reports and settlements

The Department said it did not dedicate resources to verify the accuracy of the information submitted by providers. The Department said it has never implemented a consistent process for requesting detailed payroll records from providers for reconciling to cost records. The Department also said it performed no monitoring to confirm if providers comply with cost-report instructions.

During the audit period, the Department issued guidance to providers to request an exception to credit the cost of overtime on their cost reports when calculating Settlement A (hours paid minus hours provided). This practice was not described in its Core waiver with CMS or Department policy.

Employee timesheets

The Department does not perform procedures to determine if a client received their assessed level of support hours, or reconcile the payments to provider timesheets. Rather, it relies on the cost settlement process to determine if a provider delivered the total number of contracted hours to all clients in their agency during the calendar year.

A provider that provides services at multiple locations said it did not keep detailed timesheet records by employees because of changes in administrative personnel or the records were lost. Another provider stated it does not track hours by client or household because it settles its hours for the entire agency at the end of the year.

Duplicate payments

We found duplicate payments were made to providers because an edit in the Department's payment system had not been activated to prevent claims on the same date of service for differing amounts.

Effect of Condition and Questioned Costs

Cost reports and settlements

We are questioning \$1,082,187 that was paid to the five providers when their detailed payroll records did not support the hours reported on their cost reports. The federal share of these questioned costs is \$541,093.

We are also questioning \$2,778,899 for the 35 providers who were paid for more direct service hours than they reported on their cost reports. The federal share of these questioned costs is \$1,389,450. These amounts include the Department's exception for overtime consideration.

Employee timesheet

When reconciling household schedules to employee timesheets, we identified 986 days of a total of 2,469 days when clients did not receive the number of hours providers reported to the Department they planned to provide to clients. We also identified 186 days of a total of 2,469 days when employee timesheets did not show that households assessed to receive 24 hours of support were provided 24 hours of support.



We are questioning \$106,769 when we could not determine clients received their planned hours of support. The federal share of these questioned costs is \$53,384.

Duplicate payments

We are questioning \$2,041, which is the federal share of 10 duplicate payments identified by the audit.

Summary of questioned costs

In total, we identified \$3,971,937 in known questioned costs. The federal share of these known questioned costs is \$1,985,968.

Because a statistical sampling method was used to select the 69 cost reports examined in the audit, we estimate the total improper payments to be \$5,211,292. The federal share of the estimated improper payments totals \$2,605,646.

Because a statistical sampling method was used to select the employee timesheets examined in the audit, we estimate the total improper payments to be \$51,933,276. The federal share of the estimated improper payments totals \$25,966,638.

The table below summarizes, by audit area, the known questioned costs and likely improper payments:

Audit area	Known questioned costs (state and federal)	Known questioned costs – federal portion only	Likely improper payments (state and federal)	Likely improper payments – federal portion only
Cost reports	\$3,861,086	\$1,930,543	\$5,211,292	\$2,605,646
Timesheets	\$106,769	\$53,384	\$51,933,276	\$25,966,638
Duplicate payments	\$4,082	\$2,041	-	-
Totals	\$3,971,937	\$1,985,968	\$57,144,568	\$28,572,284

We question costs when we find an agency has not complied with grant regulations or when it does not have adequate documentation to support its expenditures.

Our sampling methodology meets statistical sampling criteria under generally accepted auditing standards in AU-C 530.05. It is important to note that the sampling technique we used is intended to support our audit conclusions by determining if expenditures complied with program requirements in all material respects. Accordingly, we used an acceptance sampling formula designed to provide a high level of assurance, with a 95 percent confidence of whether exceptions exceeded our materiality threshold. Our audit report and finding reflects this conclusion. However, the likely improper payment projections are a point estimate and only represent our “best estimate of total questioned costs” as required by 2 CFR 200.516(3). To ensure a representative sample, we stratified the population by dollar amount.

Recommendations

We recommend the Department:

- Implement procedures to verify if information submitted by providers is accurate and conforms with generally accepted accounting principles
- Establish consistent activities for monitoring providers to ensure they comply with cost report instructions

- Discontinue the practice of crediting providers for the cost of overtime when calculating Settlement A
- Establish policy and monitoring activities to ensure individual clients receive their assessed hours of support
- Activate the system edit that prevents duplicate payments to supported living providers
- Seek recovery of overpayments made to providers identified by the audit
- Consult with the U.S. Department of Health and Human Services regarding whether the questioned costs identified by the audit should be repaid

Department's Response

The Department partially concurs with the finding.

As stated in previous findings, RCW 71A.12.060 provides the Secretary the authority to authorize payments for individuals in community residential programs. The system is designed to allow for resource flexibility by the Supporting Living (SL) provider throughout the year to enable the provider to efficiently meet the changing needs of the individual clients. The Department requires that over the course of a calendar year, clients receive all authorized instruction and support services (ISS) hours.

SL providers are required to complete an annual cost report. The cost report reconciles ISS hours and dollars authorized to ISS hours and dollars provided. The SL provider attests to the accuracy of the cost report. A settlement is issued to any SL provider who fails to meet the standards as prescribed in DDA Policy 6.04.

Cost Reports and Settlements

Rates are established through a rate assessment process which includes a method to adjust for the sharing of support hours within households or clusters. The assessment also includes a method to account for needed supports that occur on an infrequent basis over time, such as weekly, monthly or annual events. All of these items are factored into calculating a daily rate for the individual client. The cost reports are not used to provide information to establish rates or allocate appropriate funds from the Legislature or the Department.

During the cost settlement process the Department works in tandem with the provider to document and adequately verify that the records, such as payroll records, are correct. The analysts may request additional supporting documentation during the process of cost settlement. During this audit, we do not believe that the State Auditor's Office (SAO) requested additional supporting or clarifying documentation from providers.

In relation to provider employees not being properly categorized, Department policy 6.04 states that for staff who perform both administrative/ non-staff functions and ISS, the service provider may include that portion of the employee's hours that are dedicated to ISS function. In order to have accurately reviewed the job classifications, the auditors would have had to review every job description. The Department believes this in-depth review was not completed during the audit. In determining which payments were not allowed, it appears that SAO relied upon the job title rather than the job functions of a position. For example, the staff with the job title of accountant or representative payee may support clients with their finances.

Documents provided by SAO show some of the providers' record keeping does not adequately support the hours. Training to the providers will be offered and will focus on having adequate back up information to support the ISS expenses. The Developmental Disabilities Administration's (DDA) Rate Unit will continue to review a targeted sample of provider records to evaluate whether supporting documentation is adequate.

The DDA Rate Analyst team will continue to complete desk audits. When payment discrepancies are identified, Department staff work with the provider to address the payment discrepancies. This ensures the adequate rates are being paid and many of the over/under payments are addressed prior to receiving the cost reports.

The Department will continue to use its sampling method to verify that information submitted by providers is accurate. This sampling method combines statistical sampling with risk assessment in order to determine a sample of agencies from whom additional documentation will be requested. The additional documentation is used to verify ISS costs. For the upcoming 2018 cost report review the Department intends the sample size to be approximately one quarter of the supported living agencies.

The Department has the authority to reimburse the service provider for services delivered. The Department can grant an exception to the payment rate. The hours purchased at the higher benchmark may be adjusted for the total hours purchased. Overtime costs are necessary to adequately support clients to meet their health and safety needs.

The Department will continue to use its authority to consider provider circumstances, such as overtime and grant exceptions as necessary when calculating Settlement.

Current policy and monitoring activities will remain in place to ensure individual client assessed support needs are met.

Employee Timesheets:

The discrepancy of hours written in the report does not take into consideration that the rate assessment is based on a client's daily, weekly and annual needs for support services.

Support services such as medical appointments and essential shopping are not always done on a daily basis; rather, they are evaluated and spread out over the entire year. For example, a client assessed at 15 hours a day, or 450 a month may have three annual medical appointments that take an additional 24 hours of support during one month. The algorithm factors that in for the entire year to determine the daily rate. This also would be the case for other supports that do not occur daily. The daily rate encompasses these support hours. The staffing plan is based on an average of the client's assessed needs and is a snapshot. The staffing plan is not intended to be a reflection of the daily hours provided. DDA does not believe that the audit accounted for this consideration.

In regard to provider poor record keeping, DDA concurs with the finding.

Duplicate Payments

The Department concurs with the duplicate payment finding. This occurred due to an issue with an edit in ProviderOne. DDA will continue to work with HCA to explore remedies. DDA will process overpayments for the duplicate payments identified in this audit.

Auditor's Concluding Remarks

During the audit, we worked directly with providers to request their detailed payroll information and staff schedules and performed an independent reconciliation of their cost reports. Department staff who reconcile the cost reports said they do not have procedures in place to verify or review the accuracy of provider cost reports. Had such procedures been in place, we would have reviewed them as part of the audit. We did review the Department's desk audit process, which reconciles hours a provider attested were provided to all clients in the agency to the provider's payment data. The Department does not verify whether the information is accurate.

Regarding our review of the categorization of ISS employee hours in provider cost report schedules, we did not question costs because the 43 out of 69 sampled providers did not properly classify their employees in their cost reports. We included this in the finding because, in its instructions to providers, the Department required the information be submitted when requested, and it was not provided 62 percent of the time.

When reconciling employee timesheets, we requested that providers supply us with the job classification for all employees who provided direct support hours to clients in the sample. If we were unsure of an employee's job classification and provision of hours, we contacted providers directly to seek clarification.

The Department did not provide any information during the audit about its statistically sampling method used to verify provider information.

We questioned costs when providers were paid for hours it did not provide to clients. We acknowledge the Department decided to issue some providers a credit when their employees worked overtime. This credit should have been accounted for when calculating Settlement B (total payments to providers minus cost to provide the services), not Settlement A (total hours paid to providers minus the actual hours provided to clients).

We reaffirm our finding and will follow up in our next audit.

Applicable Laws and Regulations

Title 2 U.S. Code of Federal Regulations Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance) establishes the following applicable requirements:

Section 200.53 Improper Payments states:

- (a) *Improper payment* means any payment that should not have been made or that was made in an incorrect amount (including overpayments and underpayments) under statutory, contractual, administrative, or other legally applicable requirements; and
- (b) *Improper payment* includes any payment to an ineligible party, any payment for an ineligible good or service, any duplicate payment, any payment for a good or service not received (except for such payments where authorized by law), any payment that does not account for credit for applicable discounts, and any payment where insufficient or lack of documentation prevents a reviewer from discerning whether a payment was proper.

Section 200.303 Internal controls, states in part:

The non-Federal entity must:

- (a) Establish and maintain effective internal control over the Federal award that provides reasonable assurance that the non-Federal entity is managing the Federal award in compliance with Federal statutes, regulations, and the terms and conditions of the Federal award. These internal controls should be in compliance with guidance in “Standards for Internal Control in the Federal Government” issued by the Comptroller General of the United States or the “Internal Control Integrated Framework”, issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).
- (b) Comply with Federal statutes, regulations, and the terms and conditions of the Federal awards.
- (d) Take prompt action when instances of noncompliance are identified including noncompliance identified in audit findings.

Section 200.403 Factors affecting Allowability of costs.

Except where otherwise authorized by statute, costs must meet the following general criteria in order to be allowable under Federal awards.

- (a) Be necessary and reasonable for the performance of the Federal award and be allocable thereto under these principles.
- (b) Conform to any limitations or exclusions set forth in these principles or in the Federal award as to types or amount of cost items.
- (c) Be consistent with policies and procedures that apply uniformly to both federally-financed and other activities of the non-Federal entity.
- (d) Be accorded consistent treatment. A cost may not be assigned to a Federal award as a direct cost if any other cost incurred for the same purpose in like circumstances has been allocated to the Federal award as an indirect cost.
- (e) Be determined in accordance with generally accepted accounting principles (GAAP), except, for state and local governments and Indian tribes only, as otherwise provided for in this part.

- (f) Not be included as a cost or used to meet cost sharing or matching requirements of any other federally-financed program in either the current or a prior period. See also §200.306 Cost sharing or matching paragraph (b).
- (g) Be adequately documented. See also §§200.300 Statutory and national policy requirements through 200.309 Period of performance of this part.

Section 200.410 Collection of unallowable costs.

Payments made for costs determined to be unallowable by either the Federal awarding agency, cognizant agency for indirect costs, or pass-through entity, either as direct or indirect costs, must be refunded (including interest) to the Federal Government in accordance with instructions from the Federal agency that determined the costs are unallowable unless Federal statute or regulation directs otherwise. See also Subpart D— Post Federal Award Requirements of this part, §§200.300 Statutory and national policy requirements through 200.309 Period of performance.

Section 200.516 Audit findings, states in part:

- (a) *Audit findings reported.* The auditor must report the following as audit findings in a schedule of findings and questioned costs:
 - (1) Significant deficiencies and material weaknesses in internal control over major programs and significant instances of abuse relating to major programs. The auditor's determination of whether a deficiency in internal control is a significant deficiency or material weakness for the purpose of reporting an audit finding is in relation to a type of compliance requirement for a major program identified in the Compliance Supplement.
 - (2) Material noncompliance with the provisions of Federal statutes, regulations, or the terms and conditions of Federal awards related to a major program. The auditor's determination of whether a noncompliance with the provisions of Federal statutes, regulations, or the terms and conditions of Federal awards is material for the purpose of reporting an audit finding is in relation to a type of compliance requirement for a major program identified in the compliance supplement.
 - (3) Known questioned costs that are greater than \$25,000 for a type of compliance requirement for a major program. Known questioned costs are those specifically identified by the auditor. In evaluating the effect of questioned costs on the opinion on compliance, the auditor considers the best estimate of total costs questioned (likely questioned costs), not just the questioned costs specifically identified (known questioned costs). The auditor must also report known questioned costs when likely questioned costs are greater than \$25,000 for a type of compliance requirement for a major program. In reporting questioned costs, the auditor must include information to provide proper perspective for judging the prevalence and consequences of the questioned costs.

Title 42 U.S. Code of Federal Regulations Part 433, State Fiscal Administration, Subpart F – Refunding of Federal Share of Medicaid Overpayments to Providers

Section 433.300 Basis, states in part:

This subpart implements -

- (a) Section 1903(d)(2)(A) of the Act, which directs that quarterly Federal payments to the States under title XIX (Medicaid) of the Act are to be reduced or increased to make adjustment for prior overpayments or underpayments that the Secretary determines have been made.
- (b) Section 1903(d)(2)(C) and (D) of the Act, which provides that a State has 1 year from discovery of an overpayment for Medicaid services to recover or attempt to recover the overpayment from the provider before adjustment in the Federal Medicaid payment to the State is made; and that adjustment will be made at the end of the 1-year period, whether or not recovery is made, unless the State is unable to recover from a provider because the overpayment is a debt that has been discharged in bankruptcy or is otherwise uncollectable.

Section 433.316 When discovery of overpayment occurs and its significance.

- (a) *General rule.* The date on which an overpayment is discovered is the beginning date of the 1-year period allowed for a State to recover or seek to recover an overpayment before a refund of the Federal share of an overpayment must be made to CMS.
- (b) *Requirements for notification.* Unless a State official or fiscal agent of the State chooses to initiate a formal recoupment action against a provider without first giving written notification of its intent, a State Medicaid agency official or other State official must notify the provider in writing of any overpayment it discovers in accordance with State agency policies and procedures and must take reasonable actions to attempt to recover the overpayment in accordance with State law and procedures.
- (c) *Overpayments resulting from situations other than fraud.* An overpayment resulting from a situation other than fraud is discovered on the earliest of - -
 - (1) The date on which any Medicaid agency official or other State official first notifies a provider in writing of an overpayment and specifies a dollar amount that is subject to recovery;
 - (2) The date on which a provider initially acknowledges a specific overpaid amount in writing to the Medicaid agency; or
 - (3) The date on which any State official or fiscal agent of the State initiates a formal action to recoup a specific overpaid amount from a provider without having first notified the provider in writing.
- (d) *Overpayments resulting from fraud.*
 - (1) An overpayment that results from fraud is discovered on the date of the final written notice (as defined in § 433.304 of this subchapter) of the State's overpayment determination.
 - (2) When the State is unable to recover a debt which represents an overpayment (or any portion thereof) resulting from fraud within 1 year of discovery because no final determination of the amount of the overpayment has been made under an administrative or judicial process (as applicable), including as a result of a judgment being under appeal, no adjustment shall be made in the Federal payment to such

State on account of such overpayment (or any portion thereof) until 30 days after the date on which a final judgment (including, if applicable, a final determination on an appeal) is made.

- (3) The Medicaid agency may treat an overpayment made to a Medicaid provider as resulting from fraud under subsection (d) of this section only if it has referred a provider's case to the Medicaid fraud control unit, or appropriate law enforcement agency in States with no certified Medicaid fraud control unit, as required by § 455.15, § 455.21, or § 455.23 of this chapter, and the Medicaid fraud control unit or appropriate law enforcement agency has provided the Medicaid agency with written notification of acceptance of the case; or if the Medicaid fraud control unit or appropriate law enforcement agency has filed a civil or criminal action against a provider and has notified the State Medicaid agency.
- (e) *Overpayments identified through Federal reviews.* If a Federal review at any time indicates that a State has failed to identify an overpayment or a State has identified an overpayment but has failed to either send written notice of the overpayment to the provider that specified a dollar amount subject to recovery or initiate a formal recoupment from the provider without having first notified the provider in writing, CMS will consider the overpayment as discovered on the date that the Federal official first notifies the State in writing of the overpayment and specifies a dollar amount subject to recovery.
- (f) *Effect of changes in overpayment amount.* Any adjustment in the amount of an overpayment during the 1-year period following discovery (made in accordance with the approved State plan, Federal law and regulations governing Medicaid, and the appeals resolution process specified in State administrative policies and procedures) has the following effect on the 1-year recovery period:
 - (1) A downward adjustment in the amount of an overpayment subject to recovery that occurs after discovery does not change the original 1-year recovery period for the outstanding balance.
 - (2) An upward adjustment in the amount of an overpayment subject to recovery that occurs during the 1-year period following discovery does not change the 1-year recovery period for the original overpayment amount. A new 1-year period begins for the incremental amount only, beginning with the date of the State's written notification to the provider regarding the upward adjustment.
- (g) *Effect of partial collection by State.* A partial collection of an overpayment amount by the State from a provider during the 1-year period following discovery does not change the 1-year recovery period for the balance of the original overpayment amount due to CMS.
- (h) *Effect of administrative or judicial appeals.* Any appeal rights extended to a provider do not extend the date of discovery.

The American Institute of Certified Public Accountants defines significant deficiencies and material weaknesses in internal controls over compliance in its *Codification of Statements on Auditing Standards*, section 935, Compliance Audits, as follows:

.11 For purposes of adapting GAAS to a compliance audit, the following terms have the meanings attributed as follows: ...

Deficiency in internal control over compliance. A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance on a timely basis. A deficiency in design exists when (a) a control necessary to meet the control objective is missing, or (b) an existing control is not properly designed so that, even if the control operates as designed, the control objective would not be met. A deficiency in operation exists when a properly designed control does not operate as designed or the person performing the control does not possess the necessary authority or competence to perform the control effectively.

Material weakness in internal control over compliance. A deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a compliance requirement will not be prevented, or detected and corrected, on a timely basis. In this section, a reasonable possibility exists when the likelihood of an event occurring is either reasonably possible or probable as defined as follows:

Reasonably possible. The chance of the future event or events occurring is more than remote but less than likely.

Probable. The future event or events are likely to occur.

Significant deficiency in internal control over compliance. A deficiency, or a combination of deficiencies, in internal control over compliance that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

Material noncompliance. In the absence of a definition of material noncompliance in the governmental audit requirement, a failure to follow compliance requirements or a violation of prohibitions included in the applicable compliance requirements that results in noncompliance that is quantitatively or qualitatively material, either individually or when aggregated with other noncompliance, to the affected government program.

Office of Management and Budget OMB Uniform Guidance, Compliance Supplement for 2017, *Part 4 – Agency Program Requirements, 4.93.778 Medicaid Cluster*, states in part:

General Audit Approach for Medicaid Payments

To be allowable, Medicaid costs for medical services must be (1) covered by the State plan and waivers; (2) reviewed by the State consistent with the State’s documented procedures and system for determining medical necessity of claims; (3) properly coded; and (4) paid at the rate allowed by the State plan. Additionally, Medicaid costs must be net of beneficiary cost-sharing obligations and applicable credits (e.g., insurance, recoveries from other third parties who are responsible for covering the Medicaid costs, and drug rebates), paid to eligible providers, and only provided on behalf of eligible individuals.

Department of Social and Health Services - Application for a §1915(c) Home and Community – Based Services Waiver, approved in 2015.

Appendix I: Financial Accountability

I-2: Rates, Billing and Claims, states in part:

a. Rate Determination Methods

Personal Care

Annual cost reports are required that itemize the cost of providing the contracted service for the calendar year. Cost reports are desk audited to determine accuracy and the reasonableness of reported costs. Reported revenue received is reconciled to DSHS/SSPS payment information to determine over/under payments for services.

Settlements are calculated by ADSA staff to determine pay back amounts in cases where providers contracted for more direct service hours than they provided, or received more reimbursement for direct care costs than was paid out. There is no settlement provisions for the non-direct care staff components of the payment rate.

Washington Administrative Code WAC 388-101D-0025

Service provider responsibilities.

- (1) Service providers must meet the requirements of:
 - (a) This chapter;
 - (b) Each contract and statement of work entered into with the department;
 - (c) Each client's individual support plan when the individual support plan identifies the service provider as responsible; and
 - (d) Each client's individual instruction and support plan.
- (2) The service provider must:
 - (a) Have a designated administrator and notify the department when there is a change in administrator;
 - (b) Ensure that clients have immediate access to staff, or the means to contact staff, at all times;
 - (c) Provide adequate staff within contracted hours to administer the program and meet the needs of clients;
 - (d) Not routinely involve clients in the unpaid instruction and support of other clients;
 - (e) Not involve clients receiving crisis diversion services in the instruction and support of other clients; and
 - (f) Retain all records and other material related to the residential services contract for six years after expiration of the contract.

Department of Social and Health Services, Developmental Disabilities Administration Policy 6.04
states in part:

POLICY

- A. Service providers shall report costs of operations for the purpose of certifying the costs of services provided and to determine any settlements due.

PROCEDURES

I. REPORTING

A. Cost Reports

- C. In order for a service provider to receive payments under the residential reimbursement system, the service provider must submit an annual DDA cost report covering the completed calendar year. Completing Cost Reports and Maintaining Records

- 2. DDA Rates Unit will analyze the submitted cost report and financial statement of each service provider to determine if this information is correct, complete, and reported and conforms with generally accepted accounting principles and the requirements of this contract and the referenced policies, rules, and regulations. If the analyst finds that the cost report or financial statements are incorrect or incomplete, DDA may make adjustments to the reported information or request that the service provider makes revisions.

II. COST REPORT COMPONENTS

A. Instruction and Support Services

- 4. DDA may request job descriptions for employees to verify the duties of the positions. Paid hours worked and payroll costs charged to ISS for cost reporting purposes must be verifiable in the service provider's records, including time sheets and schedules for actual hours worked. The number of ISS paid hours reported for any individual employee or owner of a service provider must not exceed 3,120 hours per year (designated live-in staff are exempt from this limitation.)
- 6. The cost report will include schedules to report summary totals of employee hours and costs. The provider must maintain on file the details by employee, as this information may be requested by DDA.

III. SETTLEMENT

- 1. Settlement Definition. The settlement shall be for underutilization of contracted and paid service hours and dollars in the instruction and support service cost center.

2018-059 **The Department of Social and Health Services, Aging and Long-Term Support Administration, did not have adequate internal controls over and did not comply with requirements to ensure Medicaid Community First Choice client service plans were properly approved.**

Federal Awarding Agency:	U.S. Department of Health and Human Services
Pass-Through Entity:	None
CFDA Number and Title:	93.775 State Medicaid Fraud Control Units 93.777 State Survey and Certification of Health Care Providers and Suppliers (Title XVIII) Medicare 93.778 Medical Assistance Program (Medicaid; Title XIX)
Federal Award Number:	1805WA5MAP; 1805WA5ADM; 1805WAIMPL; 1805WAINCT
Applicable Compliance Component:	Activities Allowed / Unallowed Allowable Costs/Cost Principles
Known Questioned Cost Amount:	\$1,362,413 (\$1,241,764 - personal care services) (\$120,649 - associated costs)

Background

Medicaid is a jointly funded state and federal partnership providing coverage for about 1.9 million eligible low-income Washington residents who otherwise might go without medical care. Medicaid is Washington's largest public assistance program and accounts for about one-third of the State's federal expenditures. The program spent about \$12.7 billion in federal and state funds during fiscal year 2018.

The Aging and Long-Term Support Administration within the Department of Social and Health Services (Department) offers personal care and other services to support Medicaid clients in community settings through the Community First Choice program. Clients who choose to receive services in their own home have two options for the delivery of their personal care services. One option is to have the services provided by a home care aide who is recruited, trained, employed and supervised by a home care agency. The other option is for the client to recruit, hire and supervise their own provider. This type of employee is referred to as an individual provider.

The Department uses an assessment to evaluate a client's support needs and to calculate the number of personal care hours the client is eligible to receive. During the assessment process, a person-centered service plan is developed and is required by federal regulation. Among others, the service plan must:

- Reflect the individual's strengths and preferences
- Reflect clinical and support needs
- Include identified goals and desired outcomes
- Reflect the services and supports that will help the individual to achieve identified goals
- Reflect risk factors and measures in place to minimize them

- Be distributed to the client and other people involved in the plan

For Community First Choice services to be allowable, the federal regulation also requires the plan be finalized and agreed to in writing by the individual and signed by all individuals and providers responsible for its implementation.

During the program's development at the federal level, stakeholders said it could be logistically complicated for all providers to sign the plan and asked if signatures for plan agreement could be obtained through formats other than the service plan.

Federal regulators said they expect that any provider responsible for implementing services or supports authorized in the service plan should receive and sign the individual's service plan, because this would be necessary to not only understand the level of Community First Choice services and supports needed by an individual, but also the individual's strengths, preferences, goals and desired outcomes related to the provision of the services and supports.

The state plan says the person-centered service plan will be agreed to in writing by the participant and those responsible for implementing the plan. State rules require the client (or a legal representative) to give consent for services and approve their plan of care, and allow the Department to terminate services if the plan is not signed and the service summary returned to the Department within 60 days of the client's assessment completion date. In fiscal year 2018, the state Medicaid program paid about \$1 billion to providers on behalf of Community First Choice clients.

Description of Condition

The Department's Aging and Long-Term Support Administration did not have adequate internal controls over and did not comply with requirements to ensure Medicaid Community First Choice client service plans were properly approved.

Department management did not establish adequate monitoring procedures to ensure client service plans were properly signed by Department staff and clients within 60 days of service authorization. The Department's business practice has not been designed to obtain provider signatures on client service plans.

We consider these internal control deficiencies to be a material weakness.

In the prior audit, we reported the Department's Aging and Long-Term Support Administration did not have adequate internal controls in place to ensure client service plans were properly approved. The prior audit included a review of Department and client signatures on person-centered service plans. During the current audit, we expanded our scope to include a review of provider signatures on the plans to comply with federal requirements. The prior finding number was 2017-045.

Cause of Condition

Department managers said they did not require provider signatures on the service plans. For clients who receive their services from individual providers, the Department asserts that when the provider

signs their contract, they are agreeing to carry out their responsibilities related to the client's service plan and believes this process satisfies the federal requirement related to plan signatures. The Department said it sends copies of the plan to individual providers, but they are not required to acknowledge they received or reviewed the plan.

Management acknowledged a backlog of documents being scanned into client records. The Department believes the backlog and the process in getting documents to the Document Management System unit for scanning contributed to the number of client records without a signed service summary.

Effect of Condition and Questioned Costs

We used a statistical sampling method to randomly select 86 Community First Choice clients, from a total population of 47,060 that received services from an individual provider or home care agency during the audit period. We examined the client files for evidence that the service plans had been finalized and agreed to in writing as required by federal and state regulation.

Specifically, we found:

Department signatures – 32 signature issues involving 29 clients

- The Department could not locate 22 person-centered service plan signature pages
- The Department did not sign three of the plans
- The Department signed seven plans after 60 days

Client signatures – 38 signature issues involving 31 clients

- The Department could not locate 22 person-centered service plan signature pages
- The Department did not obtain client signatures on eight of the plans
- The Department obtained signatures on eight plans after 60 days

Provider signatures – 180 signature issues involving 67

- The Department could not locate 40 person-centered service plan signature pages
- The Department did not obtain provider signatures on 138 plans
- The Department obtained signatures on two plans after 60 days

We also performed follow-up testing on our 2017 audit finding that identified 25 instances when the Department either did not monitor to ensure the plans were received within 60 days or that plans had valid Department and/or client signatures. For all of the previously reported instances, client service plans were still not complete for part or all of the current audit period.

Because some plans were not properly approved or the Department could not locate some plans, we determined the Department made \$2,187,880 in unallowable payments to providers. We are questioning \$1,241,764, which is the federal portion of the unallowable payments.

When unallowable payments are identified, federal regulations suggest auditors consider if associated costs, such as benefits, were also paid. For clients who receive their services from individual providers,

the Department pays payroll-related benefits, which are considered associated costs, on behalf of Community First Choice providers. Examples of these costs include health insurance, retirement, payroll taxes and training.

We identified at least \$213,066 in associated costs that we also consider to be unallowable. We are questioning at least \$120,649, which is the federal portion of the unallowable payments related to associated costs. The Department contracts with a vendor that manages the individual provider payroll system, called IPOne. The system is currently unable to make overpayment adjustments and until the issue is resolved, the Department will not know the exact amount of associated costs to refund to the grantor. In addition, the system has been unable to correctly calculate State Unemployment Tax Act (SUTA) taxes since it began processing payroll on April 1, 2016.

Including associated costs, the total amount we are questioning is \$2,400,946. The federal share is \$1,362,413

Estimated improper payments

Because a statistical sampling method was used to select the payments we examined, we estimate the total improper payments to be \$523,252,627. The federal share of this estimate is \$297,743,259.

For the \$523,252,627 in likely improper payments, we estimate the amount of likely associated improper payments to be \$45,375,943. The federal share of this estimate is \$25,698,442.

The following table summarizes the known questioned costs and estimated improper payments by federal or state funds.

Projection to population	Known questioned costs	Estimated improper payments
Federal expenditures	\$1,362,413	\$297,743,259
State expenditures	\$1,038,533	\$225,509,368
Total expenditures	\$2,400,946	\$523,252,627

The statistical sample used for testing was also used to test compliance with other activities allowed requirements. Because some unallowable payments we examined violated multiple areas of activities allowed some of the questioned costs reported here might also be reported in finding numbers 2018-050, 2018-051, 2018-055, 2018-056, and 2018-060

Our sampling methodology meets statistical sampling criteria under generally accepted auditing standards in AU-C 530.05. It is important to note that the sampling technique we used is intended to support our audit conclusions by determining if expenditures complied with program requirements in all material respects. Accordingly, we used an acceptance sampling formula designed to provide a very high level of assurance, with a 95 percent confidence of whether exceptions exceeded our materiality threshold. Our audit report and finding reflects this conclusion. However, the likely improper payment projections are a point estimate and only represent our “best estimate of total questioned costs” as required by 2 CFR 200.516(3). To ensure a representative sample, we stratified the population by dollar amount.

Recommendations

We recommend the Department's Aging and Long-Term Support Administration:

- Require provider signatures on person-centered service plans
- Provide additional training to staff on the federal regulation and state rule that require client service plans to be agreed to in writing
- Continue monitoring activities to ensure staff follow federal and state requirements
- Identify all associated costs related to the unallowable payments for personal care services provided by individual providers
- Consult with the U.S. Department of Health and Human Services to determine if the questioned costs identified by the audit should be repaid

Department's Response

The Department partially concurs with the finding.

The Department agrees that person-centered service plans must be signed by the Department, client, and provider responsible for its implementation. The Department disagrees with the assignment of improper payments based on whether the service plan was signed by individuals responsible for its implementation. Centers for Medicare and Medicaid Services (CMS) has provided guidance to the Department stating that the federal rules covering eligibility for services are separate from the rules on person centered service planning. The lack of a signed service plan does not make a client ineligible for services and therefore should not result in an improper payment. In all the cases reviewed by the State Auditor's Office (SAO), the Department made payments to qualified providers for covered services delivered to eligible beneficiaries.

CMS did provide guidance that in some cases it may not be possible to obtain client signatures as required by federal rules, and gave direction on steps the Department can take to comply with the rules while still authorizing services without a client's signature. Based on this guidance, effective December 2018, the Department changed its regulations to no longer require the termination of services should a client not return a signed service plan within 60 days of the completion of their assessment. As the previous rule was in conflict with federal guidance, and has subsequently been revised, the Department disagrees with the SAO's assertion that the seven service plans that were signed by a client after 60 days should result in an improper payment. In addition, the Department disagrees that the seven Department signatures and two provider signatures received after 60 days should result in exceptions. The federal and state requirements do not require a Department or provider signature within 60 days of the completion of the client's assessment.

The Department disagrees with the SAO's assertion that the Department did not require provider signatures. The Department has historically included a clause in provider contracts requiring the provider to complete all personal care tasks included in the client's person-centered service plan up to the authorized hours to the provider. Every service plan is reviewed with providers and the providers must be willing and able to complete the tasks assigned to them. All providers are required to sign the contract, and the Department had interpreted 42 CFR 441.540(b)(9) as being satisfied by this signature. The Department received guidance from CMS on March 5, 2019 notifying the Department

that this interpretation does not comply with federal rules. The Department will revise its policies and procedures to ensure providers sign the person-centered service plans in the future. The Department will also make additions to the quality assurance process to monitor compliance with obtaining provider signatures.

In January of 2017, the Department made changes to its quality assurance procedures to monitor for compliance in obtaining client signatures on service plans. If proficiency is below the CMS standard of 86%, a proficiency improvement plan will be developed. Additionally, technical upgrades have been implemented in the Comprehensive Assessment and Reporting Evaluation (CARE) assessment tool to allow the client to sign their service plan via an electronic method. The Long-Term Care manual is being revised to outline this process. There will also be training and outreach efforts to educate field staff on these new methods and on person-centered approaches to obtain a client's signature. The Department's quality assurance team, as part of its established annual audit cycle, will monitor to ensure there is a signed service plan in the Department's records, and if not, will verify that an alternate form of consent has been given by the client and what attempts were made to obtain the signature. The Department will complete targeted reviews to measure compliance and determine additional next steps necessary for increased proficiency with this requirement.

Auditor's Concluding Remarks

42 CFR, Section 441.540, states that person centered service plans must be finalized and agreed to in writing by the individual and signed by all individuals and providers responsible for its implementation.

2 CFR, Section 200.53, states that an improper payment is any payment that should not have been made under statutory, contractual, administrative, or other legally applicable requirements. We consider these payments unallowable because the Department did not obtain signatures to finalize the plans.

We reaffirm our finding and will review the status of the Department's corrective action during our next audit.

Applicable Laws and Regulations

Title 2 U.S. Code of Federal Regulations Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance) establishes the following applicable requirements:

Section 200.53 Improper Payments states:

- (a) *Improper payment* means any payment that should not have been made or that was made in an incorrect amount (including overpayments and underpayments) under statutory, contractual, administrative, or other legally applicable requirements; and
- (b) *Improper payment* includes any payment to an ineligible party, any payment for an ineligible good or service, any duplicate payment, any payment for a good or service not received (except for such payments where authorized by law), any payment that does not account for credit for applicable discounts, and any payment where insufficient or

lack of documentation prevents a reviewer from discerning whether a payment was proper.

Section 200.303 Internal controls.

The non-Federal entity must:

- (a) Establish and maintain effective internal control over the Federal award that provides reasonable assurance that the non-Federal entity is managing the Federal award in compliance with Federal statutes, regulations, and the terms and conditions of the Federal award. These internal controls should be in compliance with guidance in “Standards for Internal Control in the Federal Government” issued by the Comptroller General of the United States or the “Internal Control Integrated Framework”, issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).
- (b) Comply with Federal statutes, regulations, and the terms and conditions of the Federal awards.
- (d) Take prompt action when instances of noncompliance are identified including noncompliance identified in audit findings.

Section 200.403 Factors affecting Allowability of costs.

Except where otherwise authorized by statute, costs must meet the following general criteria in order to be allowable under Federal awards.

- (a) Be necessary and reasonable for the performance of the Federal award and be allocable thereto under these principles.
- (b) Conform to any limitations or exclusions set forth in these principles or in the Federal award as to types or amount of cost items.
- (c) Be consistent with policies and procedures that apply uniformly to both federally-financed and other activities of the non-Federal entity.
- (d) Be accorded consistent treatment. A cost may not be assigned to a Federal award as a direct cost if any other cost incurred for the same purpose in like circumstances has been allocated to the Federal award as an indirect cost.
- (e) Be determined in accordance with generally accepted accounting principles (GAAP), except, for state and local governments and Indian tribes only, as otherwise provided for in this part.
- (f) Not be included as a cost or used to meet cost sharing or matching requirements of any other federally-financed program in either the current or a prior period. See also §200.306 Cost sharing or matching paragraph (b).
- (g) Be adequately documented. See also §§200.300 Statutory and national policy requirements through 200.309 Period of performance of this part.

Section 200.410 Collection of unallowable costs.

Payments made for costs determined to be unallowable by either the Federal awarding agency, cognizant agency for indirect costs, or pass-through entity, either as direct or indirect costs, must be refunded (including interest) to the Federal Government in accordance with instructions from the Federal agency that determined the costs are unallowable unless Federal statute or regulation directs otherwise. See also Subpart D— Post Federal Award Requirements of this part, §§200.300 Statutory and national policy requirements through 200.309 Period of performance.

Section 200.516 Audit findings, states in part:

- (a) *Audit findings reported.* The auditor must report the following as audit findings in a schedule of findings and questioned costs:
- (1) Significant deficiencies and material weaknesses in internal control over major programs and significant instances of abuse relating to major programs. The auditor's determination of whether a deficiency in internal control is a significant deficiency or material weakness for the purpose of reporting an audit finding is in relation to a type of compliance requirement for a major program identified in the Compliance Supplement.
 - (2) Material noncompliance with the provisions of Federal statutes, regulations, or the terms and conditions of Federal awards related to a major program. The auditor's determination of whether a noncompliance with the provisions of Federal statutes, regulations, or the terms and conditions of Federal awards is material for the purpose of reporting an audit finding is in relation to a type of compliance requirement for a major program identified in the compliance supplement.
 - (3) Known questioned costs that are greater than \$25,000 for a type of compliance requirement for a major program. Known questioned costs are those specifically identified by the auditor. In evaluating the effect of questioned costs on the opinion on compliance, the auditor considers the best estimate of total costs questioned (likely questioned costs), not just the questioned costs specifically identified (known questioned costs). The auditor must also report known questioned costs when likely questioned costs are greater than \$25,000 for a type of compliance requirement for a major program. In reporting questioned costs, the auditor must include information to provide proper perspective for judging the prevalence and consequences of the questioned costs.

Title 42 U.S. Code of Federal Regulations Part 433, State Fiscal Administration, Subpart F – Refunding of Federal Share of Medicaid Overpayments to Providers

Section 433.300 Basis.

This subpart implements -

- (a) Section 1903(d)(2)(A) of the Act, which directs that quarterly Federal payments to the States under title XIX (Medicaid) of the Act are to be reduced or increased to make adjustment for prior overpayments or underpayments that the Secretary determines have been made.
- (b) Section 1903(d)(2)(C) and (D) of the Act, which provides that a State has 1 year from discovery of an overpayment for Medicaid services to recover or attempt to recover the overpayment from the provider before adjustment in the Federal Medicaid payment to the State is made; and that adjustment will be made at the end of the 1-year period, whether or not recovery is made, unless the State is unable to recover from a provider because the overpayment is a debt that has been discharged in bankruptcy or is otherwise uncollectable.

Section 433.316 When discovery of overpayment occurs and its significance.

- (a) *General rule.* The date on which an overpayment is discovered is the beginning date of the 1-year period allowed for a State to recover or seek to recover an overpayment before a refund of the Federal share of an overpayment must be made to CMS.
- (b) *Requirements for notification.* Unless a State official or fiscal agent of the State chooses to initiate a formal recoupment action against a provider without first giving written notification of its intent, a State Medicaid agency official or other State official must notify the provider in writing of any overpayment it discovers in accordance with State agency policies and procedures and must take reasonable actions to attempt to recover the overpayment in accordance with State law and procedures.
- (c) *Overpayments resulting from situations other than fraud.* An overpayment resulting from a situation other than fraud is discovered on the earliest of - -
 - (1) The date on which any Medicaid agency official or other State official first notifies a provider in writing of an overpayment and specifies a dollar amount that is subject to recovery;
 - (2) The date on which a provider initially acknowledges a specific overpaid amount in writing to the Medicaid agency; or
 - (3) The date on which any State official or fiscal agent of the State initiates a formal action to recoup a specific overpaid amount from a provider without having first notified the provider in writing.
- (d) *Overpayments resulting from fraud.*
 - (1) An overpayment that results from fraud is discovered on the date of the final written notice (as defined in § 433.304 of this subchapter) of the State's overpayment determination.
 - (2) When the State is unable to recover a debt which represents an overpayment (or any portion thereof) resulting from fraud within 1 year of discovery because no final determination of the amount of the overpayment has been made under an administrative or judicial process (as applicable), including as a result of a judgment being under appeal, no adjustment shall be made in the Federal payment to such State on account of such overpayment (or any portion thereof) until 30 days after the date on which a final judgment (including, if applicable, a final determination on an appeal) is made.
 - (3) The Medicaid agency may treat an overpayment made to a Medicaid provider as resulting from fraud under subsection (d) of this section only if it has referred a provider's case to the Medicaid fraud control unit, or appropriate law enforcement agency in States with no certified Medicaid fraud control unit, as required by § 455.15, § 455.21, or § 455.23 of this chapter, and the Medicaid fraud control unit or appropriate law enforcement agency has provided the Medicaid agency with written notification of acceptance of the case; or if the Medicaid fraud control unit or appropriate law enforcement agency has filed a civil or criminal action against a provider and has notified the State Medicaid agency.
- (e) *Overpayments identified through Federal reviews.* If a Federal review at any time indicates that a State has failed to identify an overpayment or a State has identified an overpayment but has failed to either send written notice of the overpayment to the provider that specified a dollar amount subject to recovery or initiate a formal recoupment from the provider without having first notified the provider in writing, CMS

will consider the overpayment as discovered on the date that the Federal official first notifies the State in writing of the overpayment and specifies a dollar amount subject to recovery.

- (f) *Effect of changes in overpayment amount.* Any adjustment in the amount of an overpayment during the 1-year period following discovery (made in accordance with the approved State plan, Federal law and regulations governing Medicaid, and the appeals resolution process specified in State administrative policies and procedures) has the following effect on the 1-year recovery period:
 - (1) A downward adjustment in the amount of an overpayment subject to recovery that occurs after discovery does not change the original 1-year recovery period for the outstanding balance.
 - (2) An upward adjustment in the amount of an overpayment subject to recovery that occurs during the 1-year period following discovery does not change the 1-year recovery period for the original overpayment amount. A new 1-year period begins for the incremental amount only, beginning with the date of the State's written notification to the provider regarding the upward adjustment.
- (g) *Effect of partial collection by State.* A partial collection of an overpayment amount by the State from a provider during the 1-year period following discovery does not change the 1-year recovery period for the balance of the original overpayment amount due to CMS.
- (h) *Effect of administrative or judicial appeals.* Any appeal rights extended to a provider do not extend the date of discovery.

The American Institute of Certified Public Accountants defines significant deficiencies and material weaknesses in internal controls over compliance in its *Codification of Statements on Auditing Standards*, section 935, Compliance Audits, as follows:

.11 For purposes of adapting GAAS to a compliance audit, the following terms have the meanings attributed as follows: ...

Material weakness in internal control over compliance. A deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a compliance requirement will not be prevented, or detected and corrected, on a timely basis. In this section, a reasonable possibility exists when the likelihood of an event occurring is either reasonably possible or probable as defined as follows:

Reasonably possible. The chance of the future event or events occurring is more than remote but less than likely.

Probable. The future event or events are likely to occur.

Significant deficiency in internal control over compliance. A deficiency, or a combination of deficiencies, in internal control over compliance that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

Material noncompliance. In the absence of a definition of material noncompliance in the governmental audit requirement, a failure to follow compliance requirements or a violation of prohibitions included in the applicable compliance requirements that results in noncompliance that is quantitatively or qualitatively material, either individually or when aggregated with other noncompliance, to the affected government program.

Title 42, Code of Federal Regulations, Section 441 Services: Requirements and Limits Applicable to Specific Services, states in part:

Section 441.540 Person-centered service plan.

- (b) The person-centered service plan. The person-centered service plan must reflect the services and supports that are important for the individual to meet the needs identified through an assessment of functional need, as well as what is important to the individual with regard to preferences for the delivery of such services and supports. Commensurate with the level of need of the individual, and the scope of services and supports available under Community First Choice, the plan must:
 - (9) Be finalized and agreed to in writing by the individual and signed by all individuals and providers responsible for its implementation.
- (c) Reviewing the person-centered service plan. The person-centered service plan must be reviewed, and revised upon reassessment of functional need, at least every 12 months, when the individual's circumstances or needs change significantly, and at the request of the individual.

Section 441.720 Independent assessment, states in part:

- (a) Requirements. For each individual determined to be eligible for the State plan HCBS benefit, the State must provide for an independent assessment of needs, which may include the results of a standardized functional needs assessment, in order to establish a service plan. In applying the requirements of section 1915(i)(1)(F) of the Act, the State must:
 - (1) Perform a face-to-face assessment of the individual by an agent who is independent and qualified as defined in § 441.730, and with a person-centered process that meets the requirements of § 441.725(a) and is guided by best practice and research on effective strategies that result in improved health and quality of life outcomes.
 - (i) For the purposes of this section, a face-to-face assessment may include assessments performed by telemedicine, or other information technology medium, if the following conditions are met:
 - (C) The individual provides informed consent for this type of assessment.
 - (3) Examine the individual's relevant history including the findings from the independent evaluation of eligibility, medical records, an objective evaluation of functional ability, and any other records or information needed to develop the person-centered service plan as required in § 441.725.
- (b) Reassessments. The independent assessment of need must be conducted at least every 12 months and as needed when the individual's support needs or circumstances change significantly, in order to revise the service plan.

Medicaid Program; Community First Choice Option, 77 Fed. Reg. 88 (May 7, 2012). *Federal Register: The Daily Journal of the United States*, Web. 7 May 2012

Comment: Another commenter indicated that the requirement for all individuals and providers to sign the plan may be onerous and logistically complicated as consumers can change providers frequently for a variety of reasons, and consumers should be able to obtain agreement from providers through formats other than the service plan.

Response: After consideration of these comments we have revised the final regulation to indicate that the plan be finalized and agreed to in writing by the individual and signed by all individuals and providers responsible for its implementation...we expect that any provider that is responsible for implementing services or supports authorized in the service plan should receive and sign the individual's service plan, as this would be necessary to not only understand the level of CFC services and supports needed by an individual, but also the individual's strengths, preferences, goals and desired outcomes related to the provision of the services and supports.

Washington Administrative Code WAC 388-106-0045 When will the department authorize my long-term care services? states in part:

The department will authorize long-term care services when you:

- (1) Are assessed using CARE;
- (2) Are found financially and functionally eligible for services including, if applicable, the determination of the amount of participation toward the cost of your care and/or the amount of room and board that you must pay;
- (3) Have given written consent for services and approved your plan of care;

Washington Administrative Code WAC 388-106-0047 When can the department terminate or deny long-term care services to me? states in part:

- (3) The department will terminate long-term care services if you do not sign and return your service summary document within sixty days of your assessment completion date.

Washington State Medicaid State Plan-Community First choice State Plan Option, states in part:

X. Person-Centered Service Plan Development Process

- a. Indicate how the service plan development process ensures that the person-centered service plan addresses the individual's goals, needs (including health care needs), and preferences, by offering choices regarding the services and supports they receive and from whom.

The person-centered service plan will be developed and implemented in accordance with 42 CFR 441.550 (b).

The person-centered service plan will be understandable to the participant, will indicate the individual and/or entity responsible for monitoring the plan, and will be agreed to in writing by the participant and those responsible for implementing the plan.

2018-060

The Department of Social and Health Services, Developmental Disabilities Administration, did not have adequate internal controls over and did not comply with requirements to ensure Medicaid Community First Choice client service plans were properly approved.

Federal Awarding Agency: U.S. Department of Health and Human Services
Pass-Through Entity: None
CFDA Number and Title: 93.775 State Medicaid Fraud Control Units
93.777 State Survey and Certification of Health Care Providers and Suppliers (Title XVIII) Medicare
93.778 Medical Assistance Program (Medicaid; Title XIX)
Federal Award Number: 1805WA5MAP; 1805WA5ADM; 1805WAIMPL; 1805WAINCT
Applicable Compliance Component: Activities Allowed / Unallowed Allowable Costs/Cost Principles
Known Questioned Cost Amount: \$1,089,551
(\$931,694 - personal care services)
(\$157,857 - associated costs)

Background

Medicaid is a jointly funded state and federal partnership providing coverage for about 1.9 million eligible low-income Washington residents who otherwise might go without medical care. Medicaid is Washington's largest public assistance program and accounts for about one-third of the State's federal expenditures. The program spent about \$12.7 billion in federal and state funds during fiscal year 2017.

The Developmental Disabilities Administration in the Department of Social and Health Services (Department) offers personal care and other services to support Medicaid clients in community settings through the Community First Choice program. Clients who choose to receive services in their own home have two options for the delivery of their personal care services. One option is to have the services provided by a home care aide who is recruited, trained, employed and supervised by a home care agency. The other option is for the client to recruit, hire and supervise their own provider. This type of employee is referred to as an individual provider.

The Department uses an assessment to evaluate a client's support and to calculate the number of personal care hours the client is eligible to receive. During the assessment process, a person-centered service plan is developed and is required by federal regulation. Among other requirements, the service plan must:

- Reflect the individual's strengths and preferences
- Reflect clinical and support needs
- Include identified goals and desired outcomes
- Reflect the services and supports that will help the individual to achieve identified goals

- Reflect risk factors and measures in place to minimize them
- Be distributed to the client and other people involved in the plan

For Community First Choice services to be allowable the federal regulation also requires the plan to be finalized and agreed to in writing by the individual and signed by all individuals and providers responsible for its implementation.

During the program's development at the federal level, stakeholders said it could be logistically complicated for all providers to sign the plan and asked if signatures for plan agreement could be obtained through formats other than the service plan.

Federal regulators responded by saying they expect that any provider responsible for implementing services or supports authorized in the service plan should receive and sign the individual's service plan, because this would be necessary to not only understand the level of Community First Choice services and supports needed by an individual, but also the individual's strengths, preferences, goals and desired outcomes related to the provision of the services and supports.

The state plan says the person centered service plan will be agreed to in writing by the participant and those responsible for implementing the plan. State rules require the client (or a legal representative) to give consent for services and approve their plan of care and allows the Department to terminate services if the plan is not signed and the service summary returned to the Department within 60 days of the client's assessment completion date. In fiscal year 2018, the state Medicaid program paid about \$1 billion to providers on behalf of Community First Choice clients.

Description of Condition

The Department's Developmental Disabilities Administration, did not have adequate internal controls over and did not comply with requirements to ensure Medicaid Community First Choice client support plans were properly approved.

Department management had not established adequate monitoring procedures to ensure client service plans were properly signed by Department staff and clients within 60 days of service authorization. The Department's business practice had not been designed to obtain provider signatures on client service plans.

We consider these internal control deficiencies to be a material weakness.

In the prior two audits, we reported the Department's Developmental Disabilities Administration did not have adequate internal controls in place to ensure client service plans were properly approved. The prior audit included a review of Department and client signatures on person-centered service plans. During the current audit, we expanded our scope to include a review of provider signatures on the plans to comply with federal requirements. The prior finding numbers were 2017-046 and 2016-043.

Cause of Condition

Department managers said they did not require provider signatures on the service plans. For clients who receive their services from individual providers, the Department asserts that when the individual provider signs their contract, they are agreeing to carry out their responsibilities related to the client's service plan. The Department said it sends copies of the plan to individual providers, but they are not required to acknowledge they received or reviewed the plan.

For clients who receive their services from home care agencies, the Department asserts that by contract, home care agencies are required to get worker signatures and it has delegated the monitoring of the contracts to Area Agencies on Aging.

Formal training was provided during the audit period, but the Department said it did not have time since the last audit to fully implement its corrective action.

Effect of Condition and Questioned Costs

We used a statistical sampling method to randomly select 86 Community First Choice clients from a total population of 14,227 that received services from an individual provider or home care agency during the audit period. We examined the client files for evidence that the service plans had been finalized and agreed to in writing as required by federal and state regulation. Specifically, we found:

Department signatures – 31 signature issues involving 22 clients

- The Department could not locate 25 person-centered service plan signature pages
- The Department did not sign two of the plans
- The Department signed four plans after 60 days

Client signatures – 31 signature issues involving 22 clients

- The Department could not locate 25 person-centered service plan signature pages
- The Department did not obtain client signatures on one plan
- The Department obtained signatures after 60 days on five plans

Provider signatures – 215 signature issues involving 68 clients

- The Department could not locate 55 person-centered service plan signature pages
- The Department did not obtain provider signatures on 155 plans
- The Department obtained signatures after 60 days on five plans

We also performed follow-up testing on seven instances that were identified during our 2017 audit when the Department either did not monitor to ensure the plans were received within 60 days or that plans had valid Department and/or client signatures. Specifically, we found:

Department signature – one signature issue involving one client

- The Department signed one plan after 60 days

Provider signatures – three signature issues involving three clients

- The Department did not obtain provider signatures on three plans

Because some plans were not properly approved or the Department could not locate some plans, we determined the Department made \$1,654,909 in unallowable payments to providers. We are questioning \$931,694, which is the federal portion of the unallowable payments.

When unallowable payments are identified, federal regulations suggest auditors consider if associated costs, such as benefits, were also paid. For clients who receive their services from individual providers, the Department pays payroll-related benefits, which are considered associated costs, on behalf of Community First Choice providers. Examples of these costs include health insurance, retirement, payroll taxes and training.

We identified at least \$279,072 in associated costs that we also consider to be unallowable. We are questioning \$157,857, which is the federal portion of the unallowable payments related to associated costs. The Department contracts with a vendor that manages the individual provider payroll system, called IPOne. The system is currently unable to make overpayment adjustments and until the issue is resolved, the Department will not know the exact amount of associated costs to refund to the grantor. In addition, the system has been unable to correctly calculate State Unemployment Tax Act (SUTA) taxes since it began processing payroll on April 1, 2016.

Including associated costs, the total amount we are questioning is \$1,933,981. The federal share is \$1,089,551

Estimated improper payments

Because a statistical sampling method was used to select the payments we examined, we estimate the total improper payments to be \$170,353,801. The federal share of this estimate is \$96,633,509.

For the \$170,353,801 in likely improper payments, we estimate the amount of likely associated improper payments to be \$25,624,714. The federal share of this estimate is \$14,637,951.

The following table summarizes the known questioned costs and estimated improper payments by federal or state funds.

Projection to population	Known questioned costs	Estimated improper payments
Federal expenditures	\$1,089,551	\$96,633,509
State expenditures	\$844,430	\$73,720,292
Total expenditures	\$1,933,981	\$170,353,801

The statistical sample used for testing was also used to test compliance with other activities allowed requirements. Because some unallowable payments we examined violated multiple areas of activities allowed some of the questioned costs reported here might also be reported in finding numbers 2018-050, 2018-051, 2018-055, 2018-056, and 2018-059.

Our sampling methodology meets statistical sampling criteria under generally accepted auditing standards in AU-C 530.05. It is important to note that the sampling technique we used is intended to support our audit conclusions by determining if expenditures complied with program requirements in all material respects. Accordingly, we used an acceptance sampling formula designed to provide a very high level of assurance, with a 95 percent confidence of whether exceptions exceeded our materiality threshold. Our audit report and finding reflects this conclusion. However, the likely improper payment projections are a point estimate and only represent our “best estimate of total questioned costs” as required by 2 CFR 200.516(3). To ensure a representative sample, we stratified the population by dollar amount.

Recommendations

We recommend the Department’s Developmental Disabilities Administration:

- Require provider signatures on person-centered service plans
- Provide additional training to staff on the federal regulation and state rule that require client service plans to be agreed to in writing
- Continue monitoring activities to ensure staff follow federal and state requirements
- Identify all associated costs related to the unallowable payments for personal care services provided by individual providers
- Consult with the U.S. Department of Health and Human Services to determine if the questioned costs identified by the audit should be repaid

Department’s Response

The Department partially concurs with the finding.

The Department agrees that it must comply with federal regulations regarding obtaining signatures on clients’ person-centered service plans. The Department does not agree that improper payments can be assigned when a person-centered service plan is not signed by an individual responsible for its implementation. Centers for Medicare and Medicaid Services (CMS) has provided guidance to the Department stating that the federal rules covering eligibility for services are separate from the rules on person-centered service planning. In all the cases reviewed by the State Auditor’s Office (SAO), the Department made payments to qualified providers for covered services delivered to eligible beneficiaries. The lack of a signed person-centered service plan does not make a client ineligible for services or a provider unqualified to provide services and therefore should not result in an improper payment.

The Department also disagrees that any signatures received after 60 days should result in exceptions. Federal regulations require signatures, but not within a specified amount of time. CMS did provide guidance that in some cases it may be difficult to obtain signatures and gave direction on steps the

Department can take to comply with the rules while still continuing services without the required signatures. Based on this guidance, effective December 2018, the Department changed its regulations for the Community First Choice Program to no longer require the termination of services should a client not return a signed person-centered service plan within 60 days of the completion of their assessment.

The Department developed a process that it believed to be sufficient to meet the federal regulation regarding provider signatures on person-centered service plans. With the implementation of the Community First Choice Program the Department purposely changed policies and processes regarding provider responsibilities in person-centered service plan implementation, in order to meet the intent of the federal regulation. The Department included a clause in provider contracts requiring the provider to complete all personal care tasks included in the client's person-centered service plan, at the direction of the client. The contract requires the provider to assure that they are willing and able to complete the tasks assigned to them in the client's person-centered service plan and indicates they will receive a copy of the person-centered service plan. The contract further states that the client's person-centered service plan is incorporated as an addendum to the contract and the provider's signature on the contract is their agreement to provide the services as outlined in the person-centered service plan. All providers are required to sign the contract. The Department received guidance from CMS on March 5, 2019, notifying the Department that this interpretation does not comply with federal rules. The Department will revise its policies and procedures to obtain providers' signatures on person-centered service plans.

The Department has quality assurance processes in place to monitor for compliance in obtaining client and Department signatures on person-centered service plans. The DDA Quality Compliance Coordination team reviews client and Department signatures from a statewide sample. The review looks for signatures and documented attempts to obtain signatures. The review occurs in an established cycle and looks for statewide proficiency in obtaining client and Department signatures. If the annual review finds that the proficiency has fallen below 86% a quality improvement plan is implemented to improve statewide performance. In addition to monitoring by the Quality Compliance Coordination team, Case Manager Supervisors monitor compliance of all staff once per month. The Department will make additions to the quality assurance process to monitor compliance with obtaining provider signatures and DDA will develop and implement a training to the field specifically designed to provide support and guidance to staff in obtaining required signatures in a person centered way in alignment with CMS guidance.

Auditor's Concluding Remarks

42 CFR, Section 441.540, states that person centered service plans must be finalized and agreed to in writing by the individual and signed by all individuals and providers responsible for its implementation.

2 CFR, Section 200.53, states an improper payment is any payment that should not have been made under statutory, contractual, administrative, or other legally applicable requirements. We consider these payments unallowable because the Department did not obtain signatures to finalize the plans.

We reaffirm our finding and will review the status of the Department's corrective action during our next audit.

Applicable Laws and Regulations

Title 2 U.S. Code of Federal Regulations Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance) establishes the following applicable requirements:

Section 200.53 Improper Payments states:

- (a) *Improper payment* means any payment that should not have been made or that was made in an incorrect amount (including overpayments and underpayments) under statutory, contractual, administrative, or other legally applicable requirements; and
- (b) *Improper payment* includes any payment to an ineligible party, any payment for an ineligible good or service, any duplicate payment, any payment for a good or service not received (except for such payments where authorized by law), any payment that does not account for credit for applicable discounts, and any payment where insufficient or lack of documentation prevents a reviewer from discerning whether a payment was proper.

Section 200.303 Internal controls.

The non-Federal entity must:

- (a) Establish and maintain effective internal control over the Federal award that provides reasonable assurance that the non-Federal entity is managing the Federal award in compliance with Federal statutes, regulations, and the terms and conditions of the Federal award. These internal controls should be in compliance with guidance in “Standards for Internal Control in the Federal Government” issued by the Comptroller General of the United States or the “Internal Control Integrated Framework”, issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).
- (b) Comply with Federal statutes, regulations, and the terms and conditions of the Federal awards.
- (d) Take prompt action when instances of noncompliance are identified including noncompliance identified in audit findings.

Section 200.403 Factors affecting Allowability of costs.

Except where otherwise authorized by statute, costs must meet the following general criteria in order to be allowable under Federal awards.

- (a) Be necessary and reasonable for the performance of the Federal award and be allocable thereto under these principles.
- (b) Conform to any limitations or exclusions set forth in these principles or in the Federal award as to types or amount of cost items.
- (c) Be consistent with policies and procedures that apply uniformly to both federally-financed and other activities of the non-Federal entity.
- (d) Be accorded consistent treatment. A cost may not be assigned to a Federal award as a direct cost if any other cost incurred for the same purpose in like circumstances has been allocated to the Federal award as an indirect cost.
- (e) Be determined in accordance with generally accepted accounting principles (GAAP), except, for state and local governments and Indian tribes only, as otherwise provided for in this part.

- (f) Not be included as a cost or used to meet cost sharing or matching requirements of any other federally-financed program in either the current or a prior period. See also §200.306 Cost sharing or matching paragraph (b).
- (g) Be adequately documented. See also §§200.300 Statutory and national policy requirements through 200.309 Period of performance of this part.

Section 200.410 Collection of unallowable costs.

Payments made for costs determined to be unallowable by either the Federal awarding agency, cognizant agency for indirect costs, or pass-through entity, either as direct or indirect costs, must be refunded (including interest) to the Federal Government in accordance with instructions from the Federal agency that determined the costs are unallowable unless Federal statute or regulation directs otherwise. See also Subpart D— Post Federal Award Requirements of this part, §§200.300 Statutory and national policy requirements through 200.309 Period of performance.

Section 200.516 Audit findings, states in part:

- (a) *Audit findings reported.* The auditor must report the following as audit findings in a schedule of findings and questioned costs:
 - (1) Significant deficiencies and material weaknesses in internal control over major programs and significant instances of abuse relating to major programs. The auditor's determination of whether a deficiency in internal control is a significant deficiency or material weakness for the purpose of reporting an audit finding is in relation to a type of compliance requirement for a major program identified in the Compliance Supplement.
 - (2) Material noncompliance with the provisions of Federal statutes, regulations, or the terms and conditions of Federal awards related to a major program. The auditor's determination of whether a noncompliance with the provisions of Federal statutes, regulations, or the terms and conditions of Federal awards is material for the purpose of reporting an audit finding is in relation to a type of compliance requirement for a major program identified in the compliance supplement.
 - (3) Known questioned costs that are greater than \$25,000 for a type of compliance requirement for a major program. Known questioned costs are those specifically identified by the auditor. In evaluating the effect of questioned costs on the opinion on compliance, the auditor considers the best estimate of total costs questioned (likely questioned costs), not just the questioned costs specifically identified (known questioned costs). The auditor must also report known questioned costs when likely questioned costs are greater than \$25,000 for a type of compliance requirement for a major program. In reporting questioned costs, the auditor must include information to provide proper perspective for judging the prevalence and consequences of the questioned costs.

Title 42 U.S. Code of Federal Regulations Part 433, State Fiscal Administration, Subpart F – Refunding of Federal Share of Medicaid Overpayments to Providers

Section 433.300 Basis.

This subpart implements -

- (a) Section 1903(d)(2)(A) of the Act, which directs that quarterly Federal payments to the States under title XIX (Medicaid) of the Act are to be reduced or increased to make adjustment for prior overpayments or underpayments that the Secretary determines have been made.
- (b) Section 1903(d)(2)(C) and (D) of the Act, which provides that a State has 1 year from discovery of an overpayment for Medicaid services to recover or attempt to recover the overpayment from the provider before adjustment in the Federal Medicaid payment to the State is made; and that adjustment will be made at the end of the 1-year period, whether or not recovery is made, unless the State is unable to recover from a provider because the overpayment is a debt that has been discharged in bankruptcy or is otherwise uncollectable.

Section 433.316 When discovery of overpayment occurs and its significance.

- (a) *General rule.* The date on which an overpayment is discovered is the beginning date of the 1-year period allowed for a State to recover or seek to recover an overpayment before a refund of the Federal share of an overpayment must be made to CMS.
- (b) *Requirements for notification.* Unless a State official or fiscal agent of the State chooses to initiate a formal recoupment action against a provider without first giving written notification of its intent, a State Medicaid agency official or other State official must notify the provider in writing of any overpayment it discovers in accordance with State agency policies and procedures and must take reasonable actions to attempt to recover the overpayment in accordance with State law and procedures.
- (c) *Overpayments resulting from situations other than fraud.* An overpayment resulting from a situation other than fraud is discovered on the earliest of - -
 - (1) The date on which any Medicaid agency official or other State official first notifies a provider in writing of an overpayment and specifies a dollar amount that is subject to recovery;
 - (2) The date on which a provider initially acknowledges a specific overpaid amount in writing to the medicaid agency; or
 - (3) The date on which any State official or fiscal agent of the State initiates a formal action to recoup a specific overpaid amount from a provider without having first notified the provider in writing.
- (d) *Overpayments resulting from fraud.*
 - (1) An overpayment that results from fraud is discovered on the date of the final written notice (as defined in § 433.304 of this subchapter) of the State's overpayment determination.
 - (2) When the State is unable to recover a debt which represents an overpayment (or any portion thereof) resulting from fraud within 1 year of discovery because no final determination of the amount of the overpayment has been made under an administrative or judicial process (as applicable), including as a result of a judgment being under appeal, no adjustment shall be made in the Federal payment to such State on account of such overpayment (or any portion thereof) until 30 days after the date on which a final judgment (including, if applicable, a final determination on an appeal) is made.
 - (3) The Medicaid agency may treat an overpayment made to a Medicaid provider as resulting from fraud under subsection (d) of this section only if it has referred a

provider's case to the Medicaid fraud control unit, or appropriate law enforcement agency in States with no certified Medicaid fraud control unit, as required by § 455.15, § 455.21, or § 455.23 of this chapter, and the Medicaid fraud control unit or appropriate law enforcement agency has provided the Medicaid agency with written notification of acceptance of the case; or if the Medicaid fraud control unit or appropriate law enforcement agency has filed a civil or criminal action against a provider and has notified the State Medicaid agency.

- (e) *Overpayments identified through Federal reviews.* If a Federal review at any time indicates that a State has failed to identify an overpayment or a State has identified an overpayment but has failed to either send written notice of the overpayment to the provider that specified a dollar amount subject to recovery or initiate a formal recoupment from the provider without having first notified the provider in writing, CMS will consider the overpayment as discovered on the date that the Federal official first notifies the State in writing of the overpayment and specifies a dollar amount subject to recovery.
- (f) *Effect of changes in overpayment amount.* Any adjustment in the amount of an overpayment during the 1-year period following discovery (made in accordance with the approved State plan, Federal law and regulations governing Medicaid, and the appeals resolution process specified in State administrative policies and procedures) has the following effect on the 1-year recovery period:
 - (1) A downward adjustment in the amount of an overpayment subject to recovery that occurs after discovery does not change the original 1-year recovery period for the outstanding balance.
 - (2) An upward adjustment in the amount of an overpayment subject to recovery that occurs during the 1-year period following discovery does not change the 1-year recovery period for the original overpayment amount. A new 1-year period begins for the incremental amount only, beginning with the date of the State's written notification to the provider regarding the upward adjustment.
- (g) *Effect of partial collection by State.* A partial collection of an overpayment amount by the State from a provider during the 1-year period following discovery does not change the 1-year recovery period for the balance of the original overpayment amount due to CMS.
- (h) *Effect of administrative or judicial appeals.* Any appeal rights extended to a provider do not extend the date of discovery.

The American Institute of Certified Public Accountants defines significant deficiencies and material weaknesses in internal controls over compliance in its *Codification of Statements on Auditing Standards*, section 935, Compliance Audits, as follows:

.11 For purposes of adapting GAAS to a compliance audit, the following terms have the meanings attributed as follows: ...

Material weakness in internal control over compliance. A deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a compliance requirement will not be prevented, or detected and corrected, on a timely basis. In this section, a reasonable possibility exists when

the likelihood of an event occurring is either reasonably possible or probable as defined as follows:

Reasonably possible. The chance of the future event or events occurring is more than remote but less than likely.

Probable. The future event or events are likely to occur.

Significant deficiency in internal control over compliance. A deficiency, or a combination of deficiencies, in internal control over compliance that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

Material noncompliance. In the absence of a definition of material noncompliance in the governmental audit requirement, a failure to follow compliance requirements or a violation of prohibitions included in the applicable compliance requirements that results in noncompliance that is quantitatively or qualitatively material, either individually or when aggregated with other noncompliance, to the affected government program.

Title 42, Code of Federal Regulations, Section 441 Services: Requirements and Limits Applicable to Specific Services, states in part:

Section 441.540 Person-centered service plan.

(b) The person-centered service plan. The person-centered service plan must reflect the services and supports that are important for the individual to meet the needs identified through an assessment of functional need, as well as what is important to the individual with regard to preferences for the delivery of such services and supports. Commensurate with the level of need of the individual, and the scope of services and supports available under Community First Choice, the plan must:

(9) Be finalized and agreed to in writing by the individual and signed by all individuals and providers responsible for its implementation.

(c) Reviewing the person-centered service plan. The person-centered service plan must be reviewed, and revised upon reassessment of functional need, at least every 12 months, when the individual's circumstances or needs change significantly, and at the request of the individual.

Section 441.720 Independent assessment, states in part:

(a) Requirements. For each individual determined to be eligible for the State plan HCBS benefit, the State must provide for an independent assessment of needs, which may include the results of a standardized functional needs assessment, in order to establish a service plan. In applying the requirements of section 1915(i)(1)(F) of the Act, the State must:

(1) Perform a face-to-face assessment of the individual by an agent who is independent and qualified as defined in § 441.730, and with a person-centered process that meets the requirements of § 441.725(a) and is guided by best practice and research on effective strategies that result in improved health and quality of life outcomes.

(i) For the purposes of this section, a face-to-face assessment may include assessments performed by telemedicine, or other information technology medium, if the following conditions are met:

(C) The individual provides informed consent for this type of assessment.

- (3) Examine the individual's relevant history including the findings from the independent evaluation of eligibility, medical records, an objective evaluation of functional ability, and any other records or information needed to develop the person-centered service plan as required in § 441.725.
- (b) Reassessments. The independent assessment of need must be conducted at least every 12 months and as needed when the individual's support needs or circumstances change significantly, in order to revise the service plan.

Medicaid Program; Community First Choice Option, 77 Fed. Reg. 88 (May 7, 2012). *Federal Register: The Daily Journal of the United States*, Web. 7 May 2012

Comment: Another commenter indicated that the requirement for all individuals and providers to sign the plan may be onerous and logistically complicated as consumers can change providers frequently for a variety of reasons, and consumers should be able to obtain agreement from providers through formats other than the service plan.

Response: After consideration of these comments we have revised the final regulation to indicate that the plan be finalized and agreed to in writing by the individual and signed by all individuals and providers responsible for its implementation...we expect that any provider that is responsible for implementing services or supports authorized in the service plan should receive and sign the individual's service plan, as this would be necessary to not only understand the level of CFC services and supports needed by an individual, but also the individual's strengths, preferences, goals and desired outcomes related to the provision of the services and supports.

Washington Administrative Code WAC 388-106-0045 When will the department authorize my long-term care services? states in part:

The department will authorize long-term care services when you:

- (1) Are assessed using CARE;
- (2) Are found financially and functionally eligible for services including, if applicable, the determination of the amount of participation toward the cost of your care and/or the amount of room and board that you must pay;
- (3) Have given written consent for services and approved your plan of care;

Washington Administrative Code 388-106-0047 When can the department terminate or deny long-term care services to me? states in part

- (3) The department will terminate long-term care services if you do not sign and return your service summary document within sixty days of your assessment completion date.

Washington State Medicaid State Plan-Community First choice State Plan Option, states in part:

X. Person-Centered Service Plan Development Process

- a. Indicate how the service plan development process ensures that the person-centered service plan addresses the individual's goals, needs (including health care needs), and

preferences, by offering choices regarding the services and supports they receive and from whom.

The person-centered service plan will be developed and implemented in accordance with 42 CFR 441.550 (b).

The person-centered service plan will be understandable to the participant, will indicate the individual and/or entity responsible for monitoring the plan, and will be agreed to in writing by the participant and those responsible for implementing the plan.

2018-061 The Military Department did not have adequate internal controls over and did not comply with federal requirements to ensure subrecipients of Disaster Grants-Public Assistance received required audits.

Federal Awarding Agency: Department of Homeland Security
Pass-Through Entity: None
CFDA Number and Title: 97.036 Disaster Grants-Public Assistance
Federal Award Number: FEMA-1671-DR; FEMA-1734-DR; FEMA-1817-DR;
FEMA-1825-DR; FEMA-1963-DR; FEMA-4056-DR;
FEMA-4083-DR; FEMA-4168-DR; FEMA-4188-DR;
FEMA-4242-DR; FEMA-4243-DR; FEMA-4249-DR;
FEMA-4253-DR ; FEMA-4309-DR
Applicable Compliance Component: Subrecipient Monitoring
Known Questioned Cost Amount: None

Background

The Disaster Grants-Public Assistance (PA) program helps state, tribal and local governments pay for responding to and recovering from disasters. Following a presidential declaration of a major disaster or an emergency, the Federal Emergency Management Agency (FEMA) provides supplemental federal disaster grants assistance for debris removal, emergency protective measures and the restoration of disaster-damaged facilities owned by states, municipalities, tribes and certain private nonprofit organizations. In Washington, the PA program agency is the Military Department (Department).

In state fiscal year 2018, the Department spent over \$34 million in federal PA funds.

Federal regulations require the Department to monitor award subrecipients' activities. This includes ensuring its subrecipients that spend \$750,000 or more in federal grant money during a fiscal year obtain a single audit. The Department must also follow up on any audit findings a subrecipient receives that might affect the federal program, and must issue a management decision within six months of the audit report's acceptance by the Federal Audit Clearinghouse. The management decision must clearly state whether the audit finding is sustained, the reasons for the decision, and whether the auditee is expected to repay disallowed costs, make financial adjustments or take other action. These requirements help ensure grant money is used for purposes that are authorized and within the provisions of contracts or grant agreements.

Department records showed that management might have had to follow up on 228 subrecipients during the audit period.

In the prior audit, we reported the Department did not have adequate internal controls over and did not comply with federal requirements to ensure subrecipients of Disaster Grants-Public Assistance received required audits. The prior finding number was 2017-052.

Description of Condition

The Department did not have adequate internal controls over and did not comply with federal requirements to ensure subrecipients of Disaster Grants-Public Assistance received required audits.

During the audit period, the Department did not determine if any subrecipients received required audits and, therefore, did not determine if audit findings were followed up on and management decisions were issued promptly.

The Department had policies specifying what monitoring was required and how to perform it, but they were not followed. Management said it was in the process of revising its policies during the audit period.

We consider these internal control weaknesses to constitute a material weakness.

Cause of Condition

While the Department took steps to improve its internal controls since the prior audit finding was issued, the resignation of a key staff member delayed the implementation of the new policies.

Effect of Condition

Without establishing adequate internal controls, the Department cannot ensure all subrecipients that met the threshold for an audit complied with federal grant requirements, and thus that it has met federal monitoring requirements.

Recommendations

To improve its monitoring of subrecipients, we recommend the Department:

- Verify all required audits occurred, follow up on all subrecipient audit findings related to the program and issue a management decision promptly
- Ensure its planned changes to internal controls are implemented

Department's Response

The Military Department discovered, as a result of the 2017 Audit, that the task of tracking and reviewing audits as required by 2 CFR 200 had been neglected since extensive staff turnover in July 2016. In response to the 2017 Audit, the Department has been working towards implementing the corrective action plan established in 2018. The Department updated the "Sub-Grantee Monitoring" policy (final policy approved November 28, 2018), which assigns data collection and monitoring roles and responsibilities to the Finance Department and to individual Grant Program Managers in the Department. The Finance Department is responsible for collecting audit data from sub-grantees, and has nearly completed documenting all relevant audits for sub-grantees that were issued grants in 2017 and 2018. Upon completion of this data collection effort, the Department will implement the next step of the corrective action plan, in which the Department will verify that all required audits occur and all

subrecipient audit findings related to the program are followed up on and where necessary management decision letters are issued promptly. New sub-grantees will be added to the audit tracker database, and followed up with annually as required, as new grants are awarded in 2019 and beyond. While this process was not in place during the 2017 and 2018 calendar years, the Department will finish implementing the new process by April 2019, and continue following it thereafter.

Auditor's Concluding Remarks

We thank the Department for its cooperation and assistance throughout the audit. We will review the status of the Department's corrective action during our next audit.

Applicable Laws and Regulations

Title 2 U.S. Code of Federal Regulations Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance) establishes the following applicable requirements:

Section 200.303 Internal controls, states in part:

The non-Federal entity must:

- (a) Establish and maintain effective internal control over the Federal award that provides reasonable assurance that the non-Federal entity is managing the Federal award in compliance with Federal statutes, regulations, and the terms and conditions of the Federal award. These internal controls should be in compliance with guidance in "Standards for Internal Control in the Federal Government" issued by the Comptroller General of the United States or the "Internal Control Integrated Framework", issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).
- (b) Comply with Federal statutes, regulations, and the terms and conditions of the Federal awards.
- (d) Take prompt action when instances of noncompliance are identified including noncompliance identified in audit findings.

Section 200.516 Audit findings, states in part:

- (a) *Audit findings reported.* The auditor must report the following as audit findings in a schedule of findings and questioned costs:
 - (1) Significant deficiencies and material weaknesses in internal control over major programs and significant instances of abuse relating to major programs. The auditor's determination of whether a deficiency in internal control is a significant deficiency or material weakness for the purpose of reporting an audit finding is in relation to a type of compliance requirement for a major program identified in the Compliance Supplement.
 - (2) Material noncompliance with the provisions of Federal statutes, regulations, or the terms and conditions of Federal awards related to a major program. The auditor's determination of whether a noncompliance with the provisions of Federal statutes, regulations, or the terms and conditions of Federal awards is material for the purpose

of reporting an audit finding is in relation to a type of compliance requirement for a major program identified in the compliance supplement.

Section 200.331 Requirements for pass-through entities, states in part:

- (d) Monitor the activities of the subrecipient as necessary to ensure that the subaward is used for authorized purposes, in compliance with Federal statutes, regulations, and the terms and conditions of the subaward; and that subaward performance goals are achieved. Pass-through entity monitoring of the subrecipient must include:
 - (3) Issuing a management decision for audit findings pertaining to the Federal award provided to the subrecipient from the pass-through entity as required by §200.521 Management decision.
- (f) Verify that every subrecipient is audited as required by Subpart F—Audit Requirements of this part when it is expected that the subrecipient's Federal awards expended during the respective fiscal year equaled or exceeded the threshold set forth in §200.501 Audit requirements.

The American Institute of Certified Public Accountants defines significant deficiencies and material weaknesses in internal controls over compliance in its *Codification of Statements on Auditing Standards*, section 935, Compliance Audits, as follows:

- .11 For purposes of adapting GAAS to a compliance audit, the following terms have the meanings attributed as follows: ...

Deficiency in internal control over compliance. A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance on a timely basis. A deficiency in design exists when (a) a control necessary to meet the control objective is missing, or (b) an existing control is not properly designed so that, even if the control operates as designed, the control objective would not be met. A deficiency in operation exists when a properly designed control does not operate as designed or the person performing the control does not possess the necessary authority or competence to perform the control effectively.

Material weakness in internal control over compliance. A deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a compliance requirement will not be prevented, or detected and corrected, on a timely basis. In this section, a reasonable possibility exists when the likelihood of the event is either reasonably possible or probable as defined as follows:

Reasonably possible. The chance of the future event or events occurring is more than remote but less than likely.

Probable. The future event or events are likely to occur.

Significant deficiency in internal control over compliance. A deficiency, or a combination of deficiencies, in internal control over compliance that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

Material noncompliance. In the absence of a definition of material noncompliance in the governmental audit requirement, a failure to follow compliance requirements or a violation of prohibitions included in the applicable compliance requirements that results in noncompliance that is quantitatively or qualitatively material, either individually or when aggregated with other noncompliance, to the affected government program.