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State Auditor

An Audit Report on Earned Federal Funds at Selected Agencies

January 31, 2008

Members of the Legislative Audit Committee:

The Department of Aging and Disability Services (DADS), the Department of Assistive and Rehabilitative Services (DARS), and the Health and Human Services Commission (HHSC) deposited and classified earned federal funds in accordance with the General Appropriations Act and Comptroller of Public Account's Fiscal Policies and Procedures No. A.017.¹ For fiscal year 2007, DADS, DARS, and HHSC deposited \$8,744,368.38, \$3,461,367.63, and \$8,964,764.42, respectively, as earned federal funds.

The types of earned federal funds vary depending on the agency and its federal programs. Earned federal funds most often are generated when an agency receives federal funds for a General Revenue expenditure that was not originally made by the agency. Most agencies with federal programs collect and deposit earned federal funds related to recovering some of the costs associated with:

- The agency's portion of the Statewide Cost Allocation Plan.
- A statement of services benefiting the agency from the Office of the Attorney General.
- A statement of services benefiting the agency from the State Auditor's Office.

The Office of the Attorney General and the State Auditor's Office provide services to state agencies, but the cost of these services are not included in the Statewide Cost Allocation Plan.

Earned Federal Funds

Earned federal funds is a state-created category of funds within the General Revenue Fund. The vast majority of funds received from the federal government are identified as federal funds in the state budget and accounting system. A fraction of the funds received from the federal government is classified and deposited in accordance with the state definition of "earned federal funds."

According to the General Appropriations Act, earned federal funds are all monies received by agencies in connection with a federally funded contract, grant, or program that are not required to be used for a specific purpose, or reimbursements received for expenditures previously made on behalf of federal programs from state funds. Typically, earned federal funds are from indirect cost allocations, interest earned on federal funds, reimbursements for costs previously paid from a nonfederal fund source, and other items such as the sale of fixed assets purchased with federal funds.

Source: Article IX, Section 6.26, General Appropriations Act (80th Legislature, Regular Session).

Earned Federal Funds at the Department of Aging and Disability Services (DADS)

DADS collected and deposited earned federal funds related to its portion of the Statewide Cost Allocation Plan, other depreciation not otherwise recovered, indirect costs and depreciation for mental retardation state schools, and interest earned on federal funds. DADS has a pre-established cost allocation plan with the federal government that states how the federal share of administrative costs is charged to state programs. Therefore, none of the federal funds received for these administrative costs are indirect cost allocations and are not earned federal funds under the General Appropriations Act definition (see text box).

¹ *Earned Federal Funds and Indirect Cost Reimbursements to the General Revenue Fund (APS 023)*, Office of the Comptroller of Public Accounts, Fiscal Year 2006-2007, (Updated 79th Legislature, 2nd Called Session).

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Auditors tested all 123 of DADS' earned federal funds transactions for fiscal year 2007 related to the agency's portion of the Statewide Cost Allocation Plan, depreciation, and indirect costs and depreciation for mental retardation state schools. All of these transactions were deposited and classified correctly as earned federal funds. DADS did not request federal funds in fiscal year 2007 for the services it received from the Office of Attorney General and the State Auditor's Office. Table 1 lists the types and amounts of earned federal funds DADS received in fiscal year 2007, as well as the object codes and appropriation numbers DADS recorded in the Uniform Statewide Accounting System (USAS).

Table 1

| Amounts of Earned Federal Funds DADS Recorded Fiscal Year 2007 ^a | | | |
|--|---------------------------|--|-----------------------|
| USAS Object Code | USAS Appropriation Number | Type of Earned Federal Funds | Amount |
| 3702 | 70000 | Depreciation | \$ 46,708.96 |
| 3972 | 70000 | Depreciation ^b | 61,573.66 |
| 3726 | 70000 | Statewide Cost Allocation Plan | 148,601.67 |
| 3972 | 70000 | Statewide Cost Allocation Plan ^b | 210,589.56 |
| 3851 | 70000 | Interest | 70,693.70 |
| 3965 | 70000 | State Schools - Indirect Costs and Depreciations | 8,206,200.83 |
| Total | | | \$8,744,368.38 |

^a DADS did not request earned federal funds related to the statements of services from the Office of the Attorney General or the State Auditor's Office in fiscal year 2007.

^b DADS receives federal funds for Medicaid programs from the Health and Human Services Commission and records them using object code 3972. DADS records the depreciation and Statewide Cost Allocation Plan amounts related to the Medicaid programs to that same object code.

Earned Federal Funds at the Department of Assistive and Rehabilitative Services (DARS)

DARS collected and deposited earned federal funds related to its portion of the Statewide Cost Allocation Plan and interest earned on federal funds. DARS has an indirect cost rate agreement with the federal government and receives federal funds to cover a percentage of its total indirect costs. However, these funds are exempt from classification as earned federal funds under Section 8.02(c) of the General Appropriations Act (79th Legislature, Regular Session), which states that federal reimbursements for expenditures paid with state funds on behalf of federal programs shall be credited to the fund from which the expenditures were originally paid. In fiscal year 2007, DARS deposited and classified the funds it received under its indirect cost rate agreement as federal funds in its administrative appropriations, which was consistent with the original expenditures. Auditors tested a sample of 20 DARS earned federal funds transactions for fiscal year 2007 related to the agency's portion of the Statewide Cost Allocation Plan. All transactions tested were deposited and classified correctly as earned federal funds.

DARS received federal funds in fiscal year 2007 for services it received from the Office of Attorney General and the State Auditor's Office. DARS originally deposited and classified these funds as federal funds, rather than as earned federal funds. Auditors brought this to the agency's attention, and DARS

agreed these funds should be earned federal funds and reclassified them. Table 2 lists the types and amounts of earned federal funds DARS recorded for fiscal year 2007.

Table 2

| Amounts of Earned Federal Funds DARS Recorded Fiscal Year 2007 | | | |
|---|---------------------------|--|-----------------------|
| USAS Object Code | USAS Appropriation Number | Type of Earned Federal Funds | Amount |
| 3726 | 70000 | Statewide Cost Allocation Plan | \$ 3,261,647.92 |
| 3851 | 70000 | Interest | 89,804.19 |
| 3550 | 13021-13024 ^a | Office of Attorney General Statement of Services | 78,748.40 |
| 3550 | 13021-13024 ^a | State Auditor's Office Statement of Services | 31,167.12 |
| Total | | | \$3,461,367.63 |
| ^a These funds were originally misclassified as "federal funds." DARS later reclassified these funds correctly as "earned federal funds." | | | |

Earned Federal Funds at the Health and Human Services Commission (HHSC)

HHSC collected and deposited earned federal funds related to its portion of the Statewide Cost Allocation Plan; depreciation for legacy agency equipment; recoupments for the Aid to Families with Dependent Children (AFDC), Temporary Assistance for Needy Families (TANF), and Food Stamp programs; an administrative fee for the Medicaid Administrative Claiming program; and services the agency received from the Office of Attorney General. HHSC did not request federal funds in fiscal year 2007 for services it received from the State Auditor's Office. Like DADS, HHSC has a cost allocation plan, and therefore, does not have any earned federal funds related to indirect cost allocations. Auditors tested all 227 earned federal fund transactions HHSC recorded for fiscal year 2007. All of these transactions were deposited and classified correctly as earned federal funds. Table 3 lists the types and amounts of earned federal funds HHSC recorded for fiscal year 2007.

Table 3

| Amounts of Earned Federal Funds HHSC Recorded Fiscal Year 2007 ^a | | | |
|--|---------------------------|--|-----------------------|
| USAS Object Code | USAS Appropriation Number | Type of Earned Federal Funds | Amount |
| 3602 | 70000 | Food Stamp Recoupments | \$ 2,307,699.79 |
| 3702 | 70000 | Depreciation | 1,458,885.63 |
| 3702 | 70000 | Medicaid Administrative Claiming Fee | 92,267.40 |
| 3702 | 70000 | AFDC-TANF Recoupments | 894,578.05 |
| 3702 | 70000 | Office of Attorney General Statement of Services | 240,762.31 |
| 3726 | 70000 | Statewide Cost Allocation Plan | 3,970,571.24 |
| Total | | | \$8,964,764.42 |
| ^a HHSC did not request earned federal funds related to the statement of services from the State Auditor's Office in fiscal year 2007. | | | |

We appreciate the cooperation received from DADS, DARS, and HHSC during this audit. If you have any questions, please contact Kelly Linder, Audit Manager, or me at (512) 936-9500.

Sincerely,

John Keel, CPA
State Auditor

cc: Mr. Albert Hawkins, Executive Commissioner, Health and
Human Services Commission
Ms. Adelaide Horn, Commissioner, Department of Aging
and Disability Services
Mr. Terrell J. Murphy, Commissioner, Department of
Assistive and Rehabilitative Services

**Summary of
Objective, Scope, and Methodology**

The objective was to audit the depositing and classification practices of earned federal funds by three agencies.

The audit scope covered financial data from September 2006 through August 2007 and classification practices from September 2006 through November 2007.

The audit methodology included interviewing DADS, DARS, and HHSC personnel; interviewing Legislative Budget Board and Office of the Comptroller of Public Accounts personnel; reviewing DADS, DARS, and HHSC documentation; analyzing Uniform Statewide Accounting System (USAS) data; reviewing processes, policies, and procedures for earned federal funds; and testing USAS user access.

Audit fieldwork was conducted from October 2007 through December 2007. We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

The following members of the State Auditor's staff performed the audit:

- Brianna Lehman (Project Manager)
- Angelica C. Martinez, CPA (Assistant Project Manager)
- Barbette J. Mays
- Gary Leach, CISA, CQA (Information Systems Audit Team)
- J. Scott Killingsworth, CIA, CGAP, CGFM (Quality Control Reviewer)
- Kelly Furgeson Linder, MSCRP, CGAP (Audit Manager)



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