

John Keel, CPA
State Auditor

A Follow-Up Audit Report on
The Department of State Health Services

August 24, 2005

Members of the Legislative Audit Committee:

The Department of State Health Services has made significant progress in implementing recommendations from a March 2003 State Auditor's Office report (*An Audit Report on the Department of Health's Implementation of a Business Improvement Plan*, SAO Report No. 03-023). That audit report was originally addressed to the former Department of Health. The Department of Health ceased to exist on September 1, 2004, and its responsibilities were assumed by the Department of State Health Services, which was created as part of the consolidation of Texas health and human services agencies under House Bill 2292 (78th Legislature). Therefore, to follow up on our 2003 report, we audited the current operations of the Department of State Health Services (Department).

Of the four recommendations on which auditors followed up, the Department has fully implemented two and substantially implemented one; its implementation of the remaining recommendation is ongoing. Specifically:

- The Department has fully implemented a recommendation to determine why expenditure adjustments were being made to correct bookkeeping errors and to minimize such adjustments. In our 2003 report, we noted that making recurrent adjustments to accounting information decreased the reliability and consistency of information provided to internal and external decision-makers. The Department has also fully implemented a recommendation to provide its staff with training on its internal accounting system.
- The Department has substantially implemented the recommendation to reconcile information in its internal accounting system with the Uniform Statewide Accounting System (USAS) in a timely manner. The Department had reconciled the two systems for the first half of fiscal year 2005 (September 2004 through February 2005) as of June 19, 2005.¹ However, the Department continues to have difficulties making corrections in a timely manner. As of the end of June 2005, the Department had not completed making the corrections identified in the reconciliation for the first half of the fiscal year—more than three months after the end of the reconciliation period.
- The Department's efforts to verify the accuracy and completeness of information in its internal accounting system are ongoing.

¹ The State Auditor's Office reported previously that the Department was unable to reconcile appropriation year 2001 internal accounting system balances with USAS balances. The Department addressed this long-standing issue by using the fiscal year 2004 ending USAS balance as the fiscal year 2005 beginning balance for its internal accounting system.

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The attachment to this letter contains detailed information regarding the status of the Department's implementation of each of the recommendations on which the State Auditor's Office followed up. The other recommendations in the 2003 report have been addressed in the following ways:

- In a March 2004 audit report (*State of Texas Financial Portion of the Statewide Single Audit Report for the Year Ended August 31, 2003*, SAO Report No. 04-555), we reported that the Department had implemented a prior recommendation to comply with federal requirements regarding the submission of indirect cost recovery plans and had partially implemented a recommendation to clarify the method for calculating the interest liability owed to the federal government. (We subsequently determined that the Department had fully implemented the latter recommendation.)
- In a March 2005 audit report (*State of Texas Financial Portion of the Statewide Single Audit Report for the Year Ended August 31, 2004*, SAO Report No. 05-555), we reported that the Department had implemented a prior recommendation to provide complete information in the Cash Management Improvement Act Report it sends to the Comptroller of Public Accounts.
- We did not follow up on certain recommendations related to organizational structure because those recommendations were no longer relevant after the consolidation under House Bill 2292.

The Department agrees with our findings, and its responses are in the attachment to this letter. We appreciate its cooperation during this audit. If you have any questions, please contact John Young, Audit Manager, or me at (512) 936-9500.

Sincerely,

John Keel, CPA
State Auditor

Attachment

cc: Mr. Albert Hawkins, Executive
 Commissioner, Health and Human
 Services Commission
Dr. Eduardo Sanchez, M.P.H., Commissioner,
 Department of State Health Services

Objective, Scope, and Methodology

Our audit objective was to determine whether the Department of State Health Services has made progress in implementing recommendations and correcting deficiencies identified in *An Audit Report on the Department of Health's Implementation of a Business Improvement Plan* (SAO Report 03-023, March 2003).

The scope included actions the Department has taken since March 2003 to address relevant recommendations from SAO Report No. 03-023.

The audit methodology consisted of collecting information and documentation, performing selected tests and other procedures, analyzing and evaluating the results of the tests, and conducting interviews.

This audit was conducted in accordance with generally accepted government auditing standards.



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Attachment

Summary of Follow-Up Results

| Definitions of Implementation Status | As Table 1 shows, of the four recommendations on which auditors followed up, the Department of State Health Services (Department) has fully implemented two and substantially implemented one. Its implementation of the remaining recommendation is ongoing (see text box for definitions of implementation status). |
|---|--|
| <ul style="list-style-type: none">▪ Fully Implemented: Successful development and use of a process, system, or policy to implement a prior recommendation▪ Substantially Implemented: Successful development but inconsistent use of a process, system, or policy to implement a prior recommendation▪ Ongoing: Successful development and consistent use of a process, system, or policy to implement a prior recommendation but implementation is not fully complete▪ Incomplete: Ongoing development of a process, system, or policy to address a prior recommendation▪ Not Implemented: Lack of a formal process, system, or policy to address a prior recommendation | |

Table 1

| Status of the Department's Implementation of Prior State Auditor's Office Recommendations | | |
|---|------------------------------|--|
| Recommendation | Implementation Status | Auditor Comments |
| The Department should ensure that it reconciles information in its internal accounting system to USAS and internal subsystems in a timely manner. | Substantially Implemented | <p>The Department has implemented procedures to reconcile its internal accounting system (the Health and Human Services Administrative System, or HHSAS) to the Uniform Statewide Accounting System (USAS). In addition, the Department had completed reconciling HHSAS and USAS for the first half of fiscal year 2005 (September 2004 to February 2005) by June 19, 2005. The Department followed its procedures on all of the 21 reconciling items that we reviewed.</p> <p>However, the Department continues to have difficulties making corrections in a timely manner. The Department had not yet made corrections, more than three months after the end of the reconciliation period, to approximately 346 (31 percent) of the 1,115 items it had identified in its reconciliation.</p> |

| Status of the Department's Implementation of Prior State Auditor's Office Recommendations | | |
|---|-----------------------|---|
| Recommendation | Implementation Status | Auditor Comments |
| The Department should verify that its internal accounting system contains accurate and complete information. | Ongoing | <p>Expenditures and liabilities were properly recorded in HHSAS and USAS, and no errors were found that would cause a material misstatement of the financial statements.</p> <p>However, of the 83 vouchers tested:</p> <ul style="list-style-type: none"> ▪ Three (3.6 percent) did not have adequate supporting documentation. These vouchers did not have authorizing signatures. In addition, the individual who entered two of these vouchers into HHSAS also had final voucher approval access. This represents a weakness in separation of duties because, typically, a single individual should not be able to both enter and approve a voucher. In addition, we could not determine who had approved these vouchers as the information in HHSAS is incomplete. HHSAS did not maintain a record of approvals for those transactions. Maintaining records of approvals is important in establishing accountability for the use of State funds. ▪ One (1.2 percent) of the vouchers had an incorrect object code. <p>Department user access to HHSAS is appropriate. However, as discussed above, one employee has access to both enter and approve vouchers. In addition, three terminated Health and Human Services Commission employees (including two contractors) still had access to HHSAS. None of these employees had accessed the system after their terminations.</p> |
| Determine why bookkeeping error adjustments are made and establish appropriate processes to ensure that adjustments are minimized. | Fully Implemented | <p>The Department has addressed the issue of using adjustments to correct bookkeeping errors. After errors are identified, the Department makes corrections in accordance with its policies and procedures.</p> <p>Expenditure adjustment activity during the period we reviewed (September 1, 2004, to April 30, 2005) was \$9.8 million. This amount was 0.7 percent of the total expenditures for that period. Expenditure documents that required adjustment during that period represented 1.3 percent of total expenditure documents, which appears reasonable.</p> |
| The Department should consider providing additional training on its internal accounting system. The Department should properly train personnel to enter accounting codes. The Department should consider a pre-test to determine the need for training and a post-test to assist with the evaluation of training. | Fully Implemented | <p>The Department has resolved the issue that led to these recommendations. We verified that Department personnel took training regarding HHSAS and USAS.</p> |

Management's Response



TEXAS DEPARTMENT OF STATE HEALTH SERVICES

EDUARDO J. SANCHEZ, M.D., M.P.H.
COMMISSIONER

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August 19, 2005

John Keel, State Auditor
State Auditor's Office
1501 N. Congress Avenue
Austin, Texas 78701

Dear Mr. Keel:

The Department of State Health Services (DSHS) appreciates the work of the State Auditor's follow-up audit of the Texas Department of Health's Business Improvement Plan (SAO Report 03-023). As noted in your report, the functions of the Texas Department of Health (TDH) were transferred to the new Department of State Health Services which became operational September 1, 2004. During that transformation period, DSHS successfully implemented two of the prior years recommendations for TDH as well as making progress on the other two. We will continue our commitment to improving DSHS financial controls and accountability.

DSHS agrees in principle with the auditor's findings and will continue our efforts to resolve the issues that have been identified in this report. DSHS would offer the following management comments concerning these items:

The Department should ensure that it reconciles information in its internal accounting system to USAS and internal subsystems in a timely manner.

Response: As noted by the auditors, DSHS has implemented policies and procedures for the timely reconciliation of our internal accounting system to USAS. The transformation to DSHS this fiscal year has created a great demand on our available resources; however, DSHS will implement a plan to have all corrections of reconciling items completed in time for an accurate Annual Financial Report (AFR) in fiscal year 2005.

Person Responsible: Wilson Day, Accounting Director

Date to be Completed: October 15, 2005

The Department should verify that its internal accounting system contains accurate and complete information.

Response: DSHS will continue to provide training and resources to staff to verify the proper recording of expenditures and liabilities. DSHS agrees that only through proper recording of this information, can we provide for an accurate financial statement.

Attachment

DSHS believes that the three (3) vouchers that did not have adequate supporting documentation was an anomaly. The vouchers in question were entered and approved prior to the September 1, 2004, to provide for payment to Community Centers at the beginning of fiscal year 2005. It appears the approval for these vouchers was overwritten when we went "live" on September 1, 2004. DSHS does not believe the unique circumstances that caused this anomaly can or will be repeated. DSHS has tested the security on numerous occasions and found that the internal accounting system properly recorded the authorizing signature for approval of each voucher.

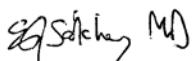
In addition, DSHS has performed on-going reviews of the security access to our internal accounting system. The auditors found only one person with both access to enter and to approve a voucher. A follow-up with HHSC security staff found that it was an error made by the security coordinator and not a situation of inadequate policies or procedures.

DSHS agrees that even though we had revoked access privileges to our computer systems for the three terminated HHSC employees; we should have also removed their security to our purchasing and human resource systems. DSHS will work with HHSC security to implement the same internal controls that exist at DSHS to any and all outside agency personnel that have access to our systems. This will include reports to security personnel of all terminations for revocation of access.

*Person Responsible: Wilson Day, Accounting Director; HHSC Security Staff
Date to be Completed: September 1, 2005*

If you have any questions or need additional information, please contact Wilson Day at 458-7674 or by e-mail at wilson.day@dshs.state.tx.us.

Sincerely,



Eduardo Sanchez, M.D., M.P.H.
Commissioner
Department of State Health Services

cc: Machelle Pharr, Chief Financial Officer
Wilson Day, Accounting Director
Tom Martinec, Internal Audit Director