

Review: 4343
Statewide Single Audit
Year Ended June 30, 2009
Department of Central Management Services

FINDINGS/RECOMMENDATIONS – 2
Repeated – 2

Implemented – 1
Accepted – 1

09-92. The auditors recommend DCMS establish a process for evaluating internal service fund balances and implement the necessary procedures to ensure these fund balances do not exceed the 60-day threshold allowed under OMB Circular A-87. DCMS should also implement procedures to ensure only expenditures meeting allowable cost criteria are used in establishing rates for expenditures charged to federal programs. (Repeated-2006)

Findings: DCMS did not establish adequate procedures to identify fund balances in excess of maximum amounts allowed under OMB Circular A-87. Auditors noted DCMS had accumulated fund balances in its Communications Revolving Fund (CRF) and Statistical Services Revolving Fund (SSRF) funds in excess of amounts allowed under OMB Circular A-87 during State fiscal years 2006, 2007 and 2008. Upon further review, the fiscal year 2009 fund balances of these funds were determined to be in excess of amounts allowed under A-87. The excess fund balances, including prior year carryforward balances were estimated to be \$9,961,000 and \$5,098,000 as of June 30, 2009 for the CRF and SSRF, respectively.

Additionally, there were several instances wherein DCMS is not properly reconciling federal internal service fund reports to its GAAP based financial statements. The majority of the differences identified represent timing differences which may have significantly altered the annual calculation of excess fund balances. As the reconciling items identified have not been associated with a specific billed service, auditors are unable to determine the impact of these items on the federal share of the excess fund balances.

In discussing these conditions with DCMS officials, they stated that their practices are compliant with A-87 guidelines.

Response: Excess Balances: The Department asserts that its excess balance adjustment practices are compliant with OMB Circular A-87 guidelines.

The Department has long employed an ongoing process to evaluate allowable balances by service for its internal service funds. Our annual SWICAP Section II submission is the culmination of an ongoing annual process involving rate developments, revenue and

expense projections, capturing and matching of costs and revenues by service center, and truing up revenues and expenses by service center and customer.

Further, the existence of excess balances is not a violation of A-87. The federal requirement is that excess balances be remedied. The Department asserts that its adjustment methods, Per A-87 Attachment C, G.4., which include negotiated settlements, are appropriate and allowable.

The Department does agree that adjustments should be made as timely as is feasible. DCMS continues to adjust rates annually to reduce exposure to excess balances. However, these annual adjustments cannot guarantee that excess balances will be entirely eliminated for all services in any given year, since rates and costs are projections. Billing credits, like cash refunds, require multiple years to apply, so the adjustment occurs no faster than a negotiated payback and requires significantly more up-front cash. Therefore, direct negotiated paybacks have always been, and will likely continue to be, a part of the federally provided and federally sanctioned remedy for excess balances.

The timeliness of direct paybacks is dependent on the federal review cycle. The paybacks are negotiated during the federal review of the annual SWICAP. The federal review cycle is not completed annually, and in some cases stretches out several years. The refunds, which are negotiated, are formally set through the federal letter of determination at the end of the review process.

In addition, the SWICAP Section I, as well as virtually all agency indirect cost rate proposals (ICRPs), are based on a two-year roll forward adjustment cycle, which recognizes the natural lag between year-end trued-up cost allocation and federal claiming. The over/under charges reported in Section II have similar FY timing limitations.

We also refer to the ASMB C-10 reference to making adjustments in the “next open fiscal period.” At the time our SWICAP Section II filing is completed, we are typically in the late third or early fourth quarter of the new FY. The State’s interpretation of the “next open fiscal period” is the next full fiscal year in which the State has the ability to adjust agency budgets to handle rate changes due to over/under billings.

Finally, the federal Dept of DHHS includes imputed interest in the payback calculations in recognition of, and as compensation for, any delay in remedying the excess balances. All excess balances for all outstanding FYs except FY09 have been remedied and approved by DHHS.

Reconciling Items: Two of the items were either recorded properly or have no federal impact:

Compensated Absences: Payroll costs are recorded in the fiscal year paid for federal reporting purposes. Per A-87, when a governmental unit uses the accrual basis of accounting, in accordance with GAAP, allowable leave costs are the lesser of the amount accrued or funded.

Inmate Commission Income: There is no federal impact as this cost center has no federal participation.

Regarding the other three items, the State concurs.

Auditors' Comment: DCMS has acknowledged the existence of excess fund balances, but believes that it is not a violation of federal regulations. Specifically, they state that negotiated settlements are appropriate and allowable. However, we believe federal regulations require DCMS to adjust rates or remit excess fund balances back to the applicable federal programs on a timely basis. DCMS' past practice of protracted negotiations and waiting for its cognizant agency to "agree to a settlement" is inconsistent with federal regulations.

Updated Response: Accepted and partially implemented. The Department negotiated paybacks with the federal DHHS to close out FY06-08 balances in April 2010. We significantly reduced FY09 balances through rates adjustments, and are in the process of negotiating FY09 results with the fed. The corrective action for this finding is an ongoing annual process involving both rates adjustments and negotiated settlements.

The Department is also adjusting accounting practices where feasible to reduce the total number of reconciling items and to document these items more accurately.

09-93. The auditors recommend DCMS implement procedures to ensure only expenditures meeting allowable cost criteria are used in establishing rates for expenditures charged to federal programs. (Repeated-2007)

Findings: DCMS recorded costs that are not allowed under OMB Circular A-87 in its internal service funds. It was noted by the auditors that other auditors had identified that DCMS had recorded unallowable costs in each of its internal service funds.

Specifically, the auditors judgmentally selected a sample of 120 cash disbursements (totaling \$4,583,603) from DCMS' internal service funds and found four of the disbursements tested (totaling \$11,287) were for costs that did not pertain to the fund in which they were recorded or were not necessary or reasonable in relation to the services provided by the fund, as summarized in the table below. Total expenditures recorded in these funds approximated \$473,121,534.

Fund	Description	Amount
SSRF	Travel to attend legislative audit committee meeting	\$457
CRF	Lodging for public information officer to assist governor's office for preparation of state budget	\$470
FMRF	Decoration of public facility – 2009 Christmas holiday decorations	\$9,861
CRF	Printing of 2000 Illinois Century Network brochures for marketing	\$499

In discussing these conditions with DCMS officials, they stated that these costs were allowable under A-87 guidelines.

Response: The Department asserts that all of the costs identified by the auditors which were subject to cost recovery were allowable under A-87 guidelines and were charged to proper funding sources. Specifically:

- The administrative travel item had been removed from the SWICAP as demonstrated to the auditors.
- The Public Information Office (PIO) is an established communications service billed through the CRF. Its activities are specifically allowable under A-87 item 1 page 15.
- Decoration of a state building falls under item 13 p. 25 in the opinion of the State.
- The Illinois Century Network (ICN) is a communications service billed through the CRF. The associated costs are allowable under A-87 item 1 page 15 and item 34 page 35.

Auditors' Comment: As discussed above, we believe the costs identified in this finding are unallowable as they were not reasonable or pertain to the fund in which they were reordered. Regarding DCMS' response above:

- DCMS could not provide documentation the administrative travel item was removed from the SWICAP.
- Travel expenses incurred related to the preparation of the State budget by the PIO are administrative expenses which should be allocated to all appropriate funds.
- Holiday decorations are not a reasonable or necessary cost for the administration of federal programs. DCMS' response above suggests the cost is allowable under OMB Circular A-87, Attachment B, Item 13 (Employee morale, health, and welfare costs). This item states, "The costs of employee information publications, health, or first-aid clinics and/or infirmaries, recreational activities, employee counseling services, and any other expenses incurred in accordance with the governmental units established practice or custom for the improvement of working conditions, employer-employee relations, employee morale, and employee performance are allowable. Such costs will be equitably apportioned to all activities of the governmental unit. ..." We do not believe holiday decorations are allowable under this section.
- The printing of the 2000 Illinois Century Network brochures appears to be an advertising cost, which we believe is unallowable under OMB Circular A-87. Specifically, OMB Circular A-87, Attachment B, item 1c, states "The only allowable advertising costs are those which are solely for 1) the recruitments of personnel required for the performance by the governmental unit of obligations arising under a

Federal award; 2) the procurement of goods and services for the performance of a Federal award; 3) the disposal of scrap or surplus materials; and 4) other specific purposes necessary to meet the requirements of the Federal award.”

Updated Response: Implemented. The Department has taken action steps to minimize the inclusion of unallowable costs and will continue to:

- Allocate allowable costs supporting multiple funds across the benefiting funds.
- Identify and eliminate non allowable expenditures from the SWCAP.