

Special Report

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**Statewide Review of  
Budget Closeout Transactions for  
Fiscal Year 2013**

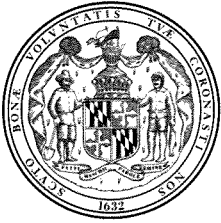
January 2014

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**OFFICE OF LEGISLATIVE AUDITS**  
DEPARTMENT OF LEGISLATIVE SERVICES  
MARYLAND GENERAL ASSEMBLY

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DEPARTMENT OF LEGISLATIVE SERVICES  
OFFICE OF LEGISLATIVE AUDITS  
MARYLAND GENERAL ASSEMBLY

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Executive Director

January 13, 2014

Thomas J. Barnickel III, CPA  
Legislative Auditor

Senator James C. Rosapepe, Co-Chair, Joint Audit Committee  
Delegate Guy J. Guzzone, Co-Chair, Joint Audit Committee  
Members of Joint Audit Committee  
Annapolis, Maryland

Ladies and Gentlemen:

We have conducted a review of the State's budget closeout transactions for the fiscal year ended June 30, 2013. Our review of closeout transactions disclosed general compliance with the applicable laws, regulations, and policies. However, we determined that certain transactions pertaining to the following agencies were not in compliance:

Department of Aging  
Maryland State Department of Education  
Department of Health and Mental Hygiene  
Maryland Health Benefit Exchange  
Department of Human Resources  
Judiciary  
Department of Juvenile Services  
Department of Veterans Affairs

Generally, the non-compliant transactions we identified suggest that additional State funds may be required to eliminate potential deficits. For example, four State agencies recorded federal or special fund revenues totaling \$32.8 million which could not be substantiated. General fund appropriations (or deficiency appropriations) will be needed to eliminate the resulting deficits if federal or special fund revenues are not available. Similar conditions were noted for these four agencies during our prior review of closeout transactions. In addition, one other agency had a federal liability of approximately \$24.1 million due to the disallowance of certain claims. Finally, excess general fund appropriations totaling \$2.3 million were not cancelled at fiscal year-end by two agencies. A summary of our findings, by agency, is included in Exhibit 1.

Five state agencies reported a total of \$34.7 million in unprovided for payables (that is, accounts payable which were not recorded in the budgetary closing

process due to a lack of available appropriation or for other reasons) as of June 30, 2013 (Exhibit 2). The expenditures related to these unprovided for payables will have to be funded with subsequent year appropriations (or through a deficiency appropriation). According to an opinion of the Attorney General, this is not a violation of State law if the General Assembly enacts a budget bill for the subsequent year containing an appropriation that can be used to fund these expenditures.

The primary purpose of this annual review is to alert the Maryland General Assembly to significant financial and budgetary closeout practices that do not comply with applicable laws, regulations, and policies. The issues identified during this review will be fully addressed, as appropriate, in our fiscal compliance audit reports on the applicable agencies, which will include relevant recommendations. We wish to acknowledge the cooperation extended to us during the course of our review by the Comptroller of Maryland's General Accounting Division and by the various State agencies.

Respectfully submitted,

A handwritten signature in black ink, reading "Thomas J. Barnickel III". The signature is written in a cursive, flowing style.

Thomas J. Barnickel III, CPA  
Legislative Auditor

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## Background Information

The Comptroller of Maryland – General Accounting Division (GAD) annually provides State agencies with instructions for completing the fiscal year-end budget closeout process. State agencies individually report to GAD their fiscal year-end closing transactions that have not been previously recorded in the State's accounting records. GAD is responsible for closing the State's accounting records on a statewide basis and for preparing the State's *Comprehensive Annual Financial Report (CAFR)*.

GAD contracts with an independent accounting firm for the purpose of expressing an opinion on the State's basic financial statements contained in the *CAFR*. In its audit report dated December 13, 2013, applicable to the fiscal year ended June 30, 2013, the firm stated that the State's basic financial statements presented fairly, in all material respects, the respective financial position of the State of Maryland as of June 30, 2013, and the respective changes in the financial position and cash flows, for the year then ended in conformity with accounting principles generally accepted in the United States of America (referred to as GAAP).

The State's *CAFR* states that, on a budgetary basis, the General Fund had an unencumbered balance of approximately \$501.9 million as of June 30, 2013. This represents a decrease of approximately \$49.3 million from the balance reported at the preceding fiscal year-end (\$551.2 million). The *CAFR* also states that the State Reserve (Revenue Stabilization Account) balance totaled \$720.2 million as of June 30, 2013.

The budgetary General Fund balance does not reflect the effect of year-end GAAP adjustments made to the State's financial statements that were prepared on a modified accrual basis of accounting. Certain GAAP adjustments, if recognized on the budgetary basis, would have reduced the aforementioned unencumbered budgetary General Fund balance of \$501.9 million. For example, one GAAP adjustment reduced the Fund balance by \$646.2 million for State and local income tax collections that were recorded as revenue for fiscal year 2013 but were applicable to future fiscal years. This adjustment was \$238.2 million larger than a similar adjustment made for the fiscal year 2012 *CAFR*. Other GAAP adjustments totaling \$34.7 million were made for liabilities incurred by State agencies during fiscal year 2013 for which general fund appropriations were not available to finance the expenditures (see Exhibit 2).





## **Introduction, Objectives, and Scope**

We conducted a review of the State's budget closeout transactions for the fiscal year ended June 30, 2013. This review was conducted under the authority of the State Government Article, Section 2-1221 of the Annotated Code of Maryland.

The objective of our review was to determine whether budget closeout transactions, for the fiscal year ended June 30, 2013, were properly supported and made in accordance with State budgetary laws, regulations, and accounting policies.

Our review consisted of tests of significant year-end transactions for 26 Departments and independent agencies to ascertain if the transactions were properly supported and made in accordance with State budgetary laws, regulations, and accounting policies. We reviewed, on a limited basis, transactions processed subsequent to June 30, 2013 to determine if the transactions were properly recorded (such as charged or credited to the proper fiscal year). We also reviewed the disposition of selected expenditure and encumbrance transactions from the fiscal year 2012 closing to ensure they were appropriately paid and remaining balances, if any, were cancelled.

As part of our current review, we contacted various officials of State agencies, as well as the independent accounting firm under contract with the State to express an opinion on its financial statements. Our review excluded public colleges and universities and transactions processed through the Transportation Trust Fund because the related financial activity does not involve the State's General Fund and/or because agencies have the authority to retain unspent funds at year-end. Our conclusions for the aforementioned objective are contained on page 9 of this report.

We also assessed the status of the 9 issues (appearing in five findings) identified in our January 22, 2013 report entitled *Statewide Review of Budget Closeout Transactions for Fiscal Year 2012*. We determined that 4 of the 9 issues had not been resolved and are repeated in this report (see Exhibit 1).

Our review was limited to the procedures necessary to accomplish the aforementioned objective. These procedures did not constitute an audit conducted in accordance with generally accepted government auditing standards (GAGAS). Had we conducted an audit in accordance with GAGAS, those standards would require the issuance of recommendations as part of our reporting process. In addition, other matters may have come to our attention that would have been

reported. We advised the appropriate agencies of our findings. Formal responses were not requested since this report contains no recommendations. Our fieldwork was conducted during the period from August 2013 to January 2014.

## **Findings**

### **Closeout Transactions**

#### **Conclusion**

Our review of State agencies' budget closeout transactions disclosed that such transactions were generally properly supported and made in accordance with State budgetary laws, regulations, and accounting policies. However, we determined that eight departments or units thereof were not in compliance primarily because certain year-end transactions were not properly recorded, could not be substantiated, or did not comply with budget closeout requirements.

#### **Revenue Transactions**

Several agencies recorded unsubstantiated revenues to offset various fund deficits. Specifically, four State agencies recorded federal fund revenues totaling approximately \$17.6 million to cover expenditures even though there was no indication that these revenues were available. In addition, special fund revenues for one of those agencies had been recorded to cover special fund expenditures totaling approximately \$15.2 million, although collection of the special fund revenue is doubtful. The use of general funds will likely be required to eliminate the deficits resulting from these transactions. Furthermore, federal fund reimbursements of \$24.1 million for one State agency were disallowed, which may also require the use of general funds to pay the resulting liability.

#### **Expenditure Transactions**

Two State agencies inappropriately encumbered general funds totaling \$2.3 million at fiscal year-end to avoid reverting unused appropriations. Another State agency did not use \$1.3 million of general funds in accordance with a budgetary law language for the appropriation. To eliminate an over-expenditure condition, a fourth State agency transferred \$600,000 of federal fund expenditures to general fund expenditures in a separate budgetary unit that had unspent general fund appropriations.

A summary of our findings, by agency, is included in Exhibit 1.

#### **Prior Year Closing Encumbrances and Accrued Expenditures**

Our review of the disposition of selected accrued expenditure and encumbrance transactions from the fiscal year 2012 closing disclosed that the transactions were properly liquidated or adequate documentation existed justifying why the transaction had not been liquidated.

## Revenue Transactions

### **Finding 1**

**The recovery of recorded federal revenues totaling approximately \$17.6 million is uncertain.**

### **Analysis**

The **Maryland State Department of Education (MSDE)**, the **Department of Human Resources (DHR)**, the **Department of Aging (DOA)**, and the **Department of Veterans Affairs (DVA)** could not substantiate their ability to collect federal fund revenues of approximately \$6.5 million, \$5.8 million, \$3.7 million, and \$1.6 million, respectively, as of June 30, 2013. If these agencies are unable to recover these federal grant funds, general funds may be needed to eliminate the resulting deficits.

### MSDE

MSDE recorded year-end federal fund revenue transactions totaling \$6.5 million related to the Library Services Technology Act (LSTA) grant expenditures made during fiscal years 2010 to 2013. MSDE has been unable to satisfy the documentation requirements for reimbursement requests established by the federal grantor agency subsequent to an audit conducted of MSDE's fiscal year 2008 and 2009 LSTA grant expenditures. The report issued by the audit firm engaged by the grantor agency questioned costs previously reimbursed to MSDE totaling \$783,866 due to the lack of adequate procedures and/or documentation to support amounts charged to the grant for subgrantees, fringe benefit costs, other direct costs, and administrative costs. This issue was commented upon in our fiscal year 2012 budgetary closeout report; at June 30, 2012, MSDE recorded federal fund revenues of \$4.7 million related to LSTA expenditures.

### DHR

DHR recorded federal fund revenue transactions of approximately \$5.8 million at June 30, 2013 related to Title XIX Medicaid claims for foster care children in residential group homes and foster care programs receiving medical services. However, DHR could not provide documentation to support any of the claims for federal Medicaid reimbursement, which would consist primarily of documentation from providers that the medical services were provided to eligible children.

### DOA

DOA recorded federal fund revenue transactions of approximately \$3.7 million at June 30, 2013 related to federal fund expenditures for the Money Follows the Person grant and the Medicaid Waiver that were incurred during fiscal year 2013 and prior years. However, as of January 3, 2014, requests for reimbursement of

these expenditures had not been prepared. This issue was commented upon in our preceding budgetary closeout report; at June 30, 2012, DOA recorded unsubstantiated federal fund revenues of \$2.9 million related to similar federal fund expenditures.

#### DVA

Federal fund revenue transactions totaling approximately \$1.6 million were primarily recorded on DVA's behalf by the Comptroller of Maryland – General Accounting Division (GAD) to eliminate deficit balances that existed in several federal programs as of June 30, 2013. Officials at DVA and GAD could not provide any documentation supporting that the year-end recorded revenues would be received. According to GAD, these deficits resulted from federal fund expenditures incurred over a number of years and the deficit had increased by \$200,000 since June 30, 2012. This issue has been commented upon in our two preceding budgetary closeout reports.

#### **Finding 2**

**Special fund revenue transactions related to assistance payments totaling approximately \$15.2 million could not be substantiated.**

#### **Analysis**

The **Department of Human Resources (DHR)** recorded special fund revenue transactions of approximately \$15.2 million at June 30, 2013 for Local Department Operations Assistance Payments. These transactions were recorded to eliminate a deficit balance in the assistance program special funds as of June 30, 2013. The deficit resulted from special fund expenditures that exceeded the available special fund revenues during fiscal years 2010 through 2013 (including \$3.7 million for fiscal year 2013). This issue was commented upon in our preceding budgetary closeout report.

#### **Finding 3**

**The Department of Health and Mental Hygiene has a liability to the federal government of \$24.1 million related to various disallowed claims.**

#### **Analysis**

The **Department of Health and Mental Hygiene – (DHMH)** has a liability to the federal government of approximately \$24.1 million for disallowed claims related to **Developmental Disabilities Administration (DDA)** residential service costs and the **Medical Care Programs Administration** drug rebate program. State general funds may be needed to repay the federal government. The Comptroller of Maryland – General Accounting Division recorded a decrease to

the General Fund in the State's fiscal year 2013 *Comprehensive Annual Financial Report* to recognize these disallowances.

As disclosed in our October 2, 2013 fiscal compliance audit report on DDA, DDA residential service costs totaling approximately \$20.6 million were disallowed by the federal Department of Health and Human Services (DHHS) – Office of the Inspector General (OIG) in its September 2013 audit report which recommended that DDA refund the overbilled amount to the federal government. On October 9, 2013, in response to the final OIG report, DHMH, on behalf of DDA, requested that DHHS consider mitigation of the monetary findings in light of substantial changes being made to management of the program and DHMH's interest in keeping as much funding as possible. As of January 8, 2014, there has been no mitigation of the liability.

In November 2013, DHHS OIG issued another audit report disallowing \$3.5 million of federal reimbursements because DHMH had not complied with federal Medicaid requirements regarding rebates when billing manufacturers for physician-administered drugs. The audit report recommended that DHMH refund the \$3.5 million.

## **Expenditure Transactions**

### **Finding 4**

**Unexpended general fund appropriations totaling approximately \$2.3 million were not cancelled at fiscal year-end.**

### **Analysis**

The **Maryland Health Benefit Exchange (MHBE)** and the **Judiciary** did not cancel unexpended general fund appropriations totaling \$1,660,000 and \$618,000, respectively, at fiscal year-end. Instead, encumbrances were inappropriately recorded to retain these funds. This practice violated the yearly closing instructions of the Comptroller of Maryland – General Accounting Division since the encumbrances did not represent actual fiscal year-end commitments by the State for goods or services and consequently would not qualify as valid encumbrances.

### **MHBE**

MHBE encumbered unused general fund appropriations totaling \$1,660,000 so that the funds could be retained and used for contractual agreements entered into during fiscal year 2014. At June 30, 2013, MHBE did not have any obligations, such as approved contracts, to support the encumbrance of these appropriations.

### Judiciary

The Judiciary encumbered general fund appropriations totaling \$618,000 for a contract that expired at June 30, 2013. During the fiscal year-end closing, the Judiciary encumbered the unspent balance of a \$750,000 contract for installing audio recording equipment. The Judiciary entered into the one-year contract on July 1, 2011 and subsequently modified the contract to extend it another year through June 30, 2013. During those two years, the Judiciary paid a total of \$132,000 for all goods and services provided under the contract.

### **Finding 5**

**The Department of Juvenile Services transferred, without proper authorization, approximately \$600,000 of federal fund expenditures related to an overspent federal grant award to general fund expenditures in a separate budgetary unit that had unspent general fund appropriations.**

### **Analysis**

The **Department of Juvenile Services (DJS)** transferred federal fund expenditures to general fund expenditures in a separate budgetary unit without proper approval. Specifically, DJS overspent a federal grant in DJS' Residential and Community Operations unit by approximately \$600,000 (expenditures exceeded federal fund appropriations and approved grant authorizations). At the end of fiscal year 2013, DJS transferred the \$600,000 in federal expenditures to its DJS Baltimore City Region Community Operations unit, which had unspent general fund appropriations to fund these costs.

DJS should have sought a budget amendment in accordance with Section 7-209 of the State Finance and Procurement Article of the Annotated Code of Maryland to transfer the available general fund appropriations to the unit that actually incurred the expenditures.

### **Finding 6**

**The Maryland State Department of Education did not use certain general fund appropriations in accordance with budgetary law language.**

### **Analysis**

The **Maryland State Department of Education (MSDE)** did not use certain general fund appropriations in accordance with budgetary law language. Specifically, MSDE inappropriately spent approximately \$1.3 million of general funds on the State Share of Foundation Program that were designated in the budget bill to be either transferred to the Guaranteed Tax Base Program (if

additional State funds were necessary for that program) or reverted to the State's General Fund. We were advised by MSDE that the budgetary language restricting the use of the general fund appropriation was not complied with because additional amounts were needed in the State Share Program to meet the State's per pupil funding specified in Section 5-202 of the Education Article of the Annotated Code of Maryland. MSDE did not seek approval for this action.

Chapter 148, Laws of Maryland, 2012 provided that \$1,376,467 of the fiscal year 2013 appropriation made for the State Share of Foundation Program shall not be spent for that purpose and instead may only be transferred to the Guaranteed Tax Base Program if additional State funds are necessary and any funds not expended for this restricted purpose shall revert to the General Fund. At fiscal year 2013 year-end, MSDE only reverted \$60,000 from the State Share of Foundation Program to the State's General fund, and none of the appropriation was transferred to the Guaranteed Tax Base Program.



## Exhibit 1

### Summary of Fiscal Year 2013 Closeout Review Findings by State Agency

Agency	Finding Number	Finding Description
<b>Maryland State Department of Education</b>	<b>1*</b> <b>6</b>	Recovery of \$6.5 million in recorded federal fund revenues is uncertain  \$1.3 million in general fund appropriations were not used in accordance with budgetary law language
<b>Department of Human Resources</b>	<b>1</b> <b>2*</b>	Recovery of \$5.8 million in recorded federal fund revenues is uncertain  \$15.2 million in unsubstantiated special fund revenue transactions were recorded
<b>Department of Aging</b>	<b>1*</b>	Recovery of \$3.7 million in recorded federal fund revenues is uncertain
<b>Department of Veterans Affairs</b>	<b>1*</b>	\$1.6 million in federal fund revenues were recorded even though related federal funds are not available
<b>Department of Health and Mental Hygiene</b>	<b>3</b>	A federal liability of approximately \$24.1 million may have to be funded with State general funds
<b>Maryland Health Benefit Exchange</b>	<b>4</b>	Unexpended general fund appropriations of \$1,660,000 were not cancelled at fiscal year-end
<b>Judiciary</b>	<b>4</b>	Unexpended general fund appropriations of \$618,000 were not cancelled at fiscal year-end
<b>Department of Juvenile Services</b>	<b>5</b>	Federal fund expenditures totaling \$600,000 were transferred to general fund expenditures in a separate budgetary unit with unspent general fund appropriations

**\* Denotes item repeated in full or part from preceding report**

## Exhibit 2

### Schedule of June 30, 2013 Unprovided for General Fund Payables According to the General Accounting Division

Agency	Amount of Reported Unprovided for Payables As of June 30, 2013
Department of Human Resources	\$20,129,118
Department of Health and Mental Hygiene	6,056,657
Maryland Higher Education Commission	3,532,896
Office of the Public Defender	2,928,034
Department of State Police	2,055,910
<b>Total</b>	<b>\$34,702,615</b>

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