

Audit Report

Department of Veterans Affairs

December 2016



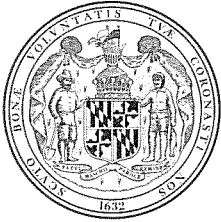
OFFICE OF LEGISLATIVE AUDITS
DEPARTMENT OF LEGISLATIVE SERVICES
MARYLAND GENERAL ASSEMBLY

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DEPARTMENT OF LEGISLATIVE SERVICES
OFFICE OF LEGISLATIVE AUDITS
MARYLAND GENERAL ASSEMBLY

Warren G. Deschenaux
Executive Director

Thomas J. Barnickel III, CPA
Legislative Auditor

December 1, 2016

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

Ladies and Gentlemen:

We have audited the Department of Veterans Affairs (DVA) for the period beginning December 8, 2012 and ending March 6, 2016. DVA assists veterans and their families and survivors in obtaining federal, State, and local benefits provided by law in recognition of their service to state and country. DVA also manages five veterans' cemeteries, maintains four veterans' war memorials, and operates and manages the Charlotte Hall Veterans Home.

Our audit disclosed that DVA did not use certain funds as intended and improperly retained funds totaling \$126,000, at the close of fiscal year 2015, that should have been reverted to the State's General Fund. DVA also had a federal fund deficit totaling approximately \$1 million at June 30, 2015, which had occurred several years earlier, but for which a deficiency appropriation was obtained during fiscal year 2016. Federal fund allowance requests were not made in a timely manner from the U.S. Department of Veterans Affairs (USDVA), and DVA has experienced significant delays in obtaining these reimbursements.

DVA did not reduce payments to the vendor operating the Charlotte Hall Veterans Home when required staffing was not provided. We estimate DVA could have reduced vendor payments by \$180,000 for the 15-month period reviewed. Finally, we noted control and record keeping deficiencies over purchases and disbursements, and cash receipts. For example, DVA did not always record collections upon receipt, and independent verifications were not performed to ensure all collections were deposited.

DVA's response to this audit is included as an appendix to this report. We wish to acknowledge the cooperation extended to us during the course of this audit by DVA.

Respectfully submitted,

A handwritten signature in black ink, appearing to read "TJ Barnickel III". The signature is stylized with a large "T" and "J" and a cursive "Barnickel III".

Thomas J. Barnickel III, CPA
Legislative Auditor

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Background Information

Agency Responsibilities

The Department of Veterans Affairs (DVA) delivers services and administers programs to assist veterans, their families, and survivors in obtaining federal, State, and local benefits provided by law in recognition of their service to the State and country. DVA provides administrative services through numerous veterans' service centers throughout the State, the United States Department of Veterans Affairs Medical Center, and the Charlotte Hall Veterans Home (CHVH), and operates and maintains five veterans' cemeteries, four veterans' war memorials, and offices in Annapolis and Baltimore. CHVH provides care for Maryland veterans who are unable to care for themselves due to disability or advancing age, or who have the need for skilled nursing care. According to the State's records, DVA's operating expenditures for fiscal year 2015 totaled approximately \$31.4 million (\$22.5 million in federal funds, \$8.2 million in general funds, and \$727,000 in special funds).

Status of Findings From Preceding Audit Report

Our audit included a review to determine the status of the seven findings contained in our preceding audit report dated December 6, 2013. We determined that DVA satisfactorily addressed four of these findings. The remaining three findings are repeated in this report.

Findings and Recommendations

Special Funds

Finding 1

The Department of Veterans Affairs (DVA) did not use certain funds as intended and improperly retained funds totaling approximately \$126,000 at the end of fiscal year 2015 that should have been reverted to the State's General Fund.

Analysis

The Department of Veterans Affairs (DVA) did not use certain funds as intended and improperly retained funds at the end of fiscal year 2015 that should have been reverted to the State's General Fund.

- DVA did not use funds recovered from veteran's families totaling \$303,000 to offset the burial costs paid for with general funds, as intended. DVA pays for burial costs of veterans' dependents using general funds and subsequently recovers a portion of these funds from veterans' families, but did not always use the recovered funds to offset the general fund expenditures. For example, during fiscal year 2014, DVA recovered \$659,000 from veterans' families but only used \$394,000 to offset the related general fund expenditures. As a result, DVA had accumulated a special fund balance of \$303,000 at the end of fiscal year 2015. These recovered funds were budgeted as special funds to be used to offset the burial costs that were paid for with general funds. DVA did not use the special funds as intended and, as a result, general funds which would otherwise have been reverted were used to cover these expenditures. Advice recently obtained from the Department of Budget and Management (DBM) and DVA attorneys general stated that DVA may retain these special funds but should only use the funds for their authorized purpose.
- DVA improperly deposited \$126,000 in energy credits received from utility companies into a special fund intended for gifts and grants for the Charlotte Hall Veterans Home (CHVH) and retained those funds at the end of fiscal year 2015. While State law provides for the retention of gifts and grants for CHVH, it does not provide for retention of the energy credits. We were advised by DBM that DVA did not have authorization to spend these funds during fiscal year 2015 and therefore these funds should have been reverted to the State's General Fund.

Recommendation 1

We recommend that DVA

- a. use the accumulated and future funds recovered from veterans' families for burial costs as intended, and**
- b. revert funds improperly retained for energy credits to the State's General Fund.**

Budget Closeout Transactions

Finding 2

Unsupported federal fund revenue transactions totaling approximately \$1 million were recorded to offset deficit balances as of June 30, 2015.

Analysis

DVA recorded federal fund revenue transactions totaling approximately \$1 million in the State's Financial Management Information System to offset deficit balances that existed in federal programs as of June 30, 2015. According to the Comptroller of Maryland – General Accounting Division (GAD), these deficits resulted from federal fund expenditures incurred during prior years dating back to at least fiscal year 2007. Management personnel at DVA could not provide any documentation supporting that the recorded federal fund revenue would be received. GAD requires that detail documentation be maintained to support revenue transactions as part of the year-end closing process.

This issue was commented upon in our preceding audit report of DVA as well as in our *Statewide Review of Budgetary Transactions* for fiscal years 2011 through 2015. During the 2016 Session of the Maryland General Assembly, DVA was provided with a \$1 million deficiency appropriation to eliminate the aforementioned deficit balance.

Recommendation 2

We recommend that DVA ensure that all year-end revenue transactions recorded in the State's Financial Management Information System are properly supported (repeat).

Federal Funds

Finding 3

DVA did not request federal fund allowances for veterans' burials from the U.S. Department of Veterans Affairs (USDVA) in a timely manner. In addition, DVA has experienced significant delays in recovering \$2.7 million in burial funds from the USDVA.

Analysis

DVA did not request federal fund allowances for veterans' burials from USDVA in a timely manner, and has experienced significant delays in recovering \$2.7 million in funds requested from the USDVA, resulting in lost interest income to the State. The State's five veterans' cemeteries are eligible to receive an allowance in an amount ranging from \$722 to \$747 for each veteran buried in a State veterans' cemetery. Each month the cemeteries submit a State application for internment allowance to DVA's Annapolis fiscal office where the applications are approved and submitted to the USDVA for payment.

Our test of 20 monthly allowance requests for burials that occurred during the period from July 2014 through February 2016, totaling \$2.6 million, disclosed that 14 requests totaling \$1.8 million were submitted 37 to 169 days later than they could have been. For example, a request for veterans' burials in January 2015, totaling \$170,000, was not submitted for payment until June 15, 2015. We were unable to determine the timeliness of 2 of the requests tested, totaling \$269,000, because the documentation on file did not contain the request dates. The 14 untimely requests resulted in lost interest income to the State of approximately \$5,000.

DVA has experienced significant delays in its reimbursement of these funds. As of May 18, 2016, DVA had not received allowances from USDVA for burial costs totaling \$2.7 million (\$1 million for fiscal year 2016; \$1 million for fiscal year 2015; \$700,000 for fiscal year 2014; and \$43,000 for fiscal year 2013). Because State funds were used to cover the costs of these expenditures, we estimate the State lost an additional \$14,000 in interest income for the aforementioned 14 untimely allowance requests. DVA made certain attempts to obtain these reimbursements; however, these attempts have not been successful. While acknowledging the amounts due, USDVA advised us that the delays in processing the requests were primarily due to turnover of its personnel responsible for processing, auditing, and paying burial payment requests.

Recommendation 3

We recommend that DVA

- a. submit allowance requests in a timely manner (such as within 30 days of the month of the burial) to the USDVA, and**
- b. continue to work with the USDVA to obtain payment for the outstanding allowance requests.**

Purchases and Disbursements

Finding 4

DVA did not always use the appropriate payment method for disbursement transactions and did not always document that goods or services were received prior to payment.

Analysis

DVA did not always use the appropriate payment method for disbursement transactions. According to the State's accounting records, during the period from July 1, 2012 through February 26, 2016, DVA processed all of its \$66.7 million in disbursement transactions on the State's Financial Management Information System using the direct payment method rather than prepare purchase orders and electronically match them with invoices and receiving reports. The majority of these transactions (\$56.5 million) were invoice payments to the vendor operating CHVH which should have been matched to the purchase order to ensure amounts paid were proper and did not exceed the maximum cost specified in the contract. Based on our review, the amounts paid to the CHVH vendor as of February 2016 did not exceed the maximum contract amount.

DVA management advised us that DVA personnel manually compared the purchase orders with vendor invoices, and documented on the invoices that goods or services were received prior to payment. However, our test of 15 transactions from fiscal years 2013 through 2016 totaling \$674,000 paid to other vendors disclosed 4 transactions totaling \$52,000 where there was no documentation that the receipt of the related goods or services had been verified prior to payment.

The Department of Information Technology's *Internal Control and Security Policy and Procedures Manual* states a match payment type should be used for purchase of services and commodities. Such an automated process ensures that invoices are only paid for purchases that were properly authorized and for goods and services that were actually received. The failure to use the proper payment method was noted in our preceding audit report.

Recommendation 4

We recommend that DVA

- a. use the appropriate online method to process payment transactions to ensure purchase orders are prepared for all applicable expenditures and matched with the related invoices and receiving reports (when applicable) prior to payment (repeat), and**
- b. adequately document that goods and services are received prior to payment.**

Finding 5

DVA did not reduce payments to the vendor operating CHVH, as permitted by the contract, when required staffing was not provided.

Analysis

DVA did not reduce payments to the vendor operating CHVH when required staffing was not provided, as permitted by the contract. Our review of the staffing reports provided by the vendor for the period from January 2015 to March 2016 disclosed two nursing positions that were vacant for the entire 15-month period and another position (Social Services Director) that was vacant for approximately 5 months. Based on the hourly rate for the three vacant positions and a 40-hour week, we estimate DVA could have reduced the payments to the vendor by approximately \$180,000 during this period.

The contract with the vendor, effective October 2010, included certain minimum staffing requirements and provided that DVA would pay the vendor a per diem for each eligible individual served. Because the level of service is largely dependent upon qualified and capable staff at the levels proposed by the vendor, the contract also provided for DVA to reduce the vendor's per diem payments for the prorated salaries of positions that were vacant for more than 45 days. DVA management advised us that vendor staffing reports were reviewed to identify vacant positions but payments had never been reduced. The contract allowed for exceptions to be approved by DVA based on circumstances in which a position could not be filled within the 45-day allowable period; however, DVA was not aware of any approved exceptions.

DVA paid the vendor approximately \$18.6 million during fiscal year 2015, which included \$13.7 million in per diem payments. The remaining vendor payments included an unrestricted State grant and reimbursement for other costs associated with the operation of CHVH and other resident activities and services.

Recommendation 5

We recommend that DVA obtain and review required staffing information from the vendor for the entire contract period and recover any amounts due for vacant positions, including those noted above.

Cash Receipts

Finding 6

DVA did not always record collections upon receipt, and deposit verifications either were not performed or were performed by individuals who processed or had access to the related collections.

Analysis

DVA did not always record collections upon receipt, and independent deposit verifications were not performed. DVA's collections were primarily received at its Annapolis fiscal office, five veterans' cemeteries, and CHVH. According to the State's records, during fiscal year 2015, DVA's collections totaled approximately \$1.8 million. Collections related to federal burial allowances, reimbursements of funeral costs from veterans' dependents, and CHVH donations.

- DVA did not record monthly burial allowances upon receipt, which totaled approximately \$764,000 during fiscal year 2015. These collections were received from the federal government at DVA's Annapolis fiscal office until April 2015 when responsibility for processing these collections was transferred to one of DVA's cemeteries. DVA deposited these funds without initially recording the collections upon receipt at either location until February 2016. In addition, there were no deposit verifications performed at these locations to ensure these funds were subsequently deposited.
- Prior to February 2016, the deposit verifications for other receipts were not independent because they were performed by individuals who processed or had access to the related collections. Although DVA implemented an independent verification of these collections in February of 2016, the verification of certain collections (related to CHVH) was not sufficient because it did not include the initial source of recordation.

Similar conditions regarding the failure to perform deposit verifications were noted in our two preceding audit reports. The Comptroller of Maryland's *Accounting Procedures Manual* requires recording of checks immediately upon receipt and that a reconciliation of the initial recordation of collections to the

amount deposited be performed by an employee independent of the cash receipts function.

Recommendation 6

We recommend that DVA ensure that

- a. all collections are recorded immediately upon receipt; and**
- b. employees independent from the cash receipts functions perform documented verifications that collections initially recorded are subsequently deposited (repeat).**

We advised DVA on accomplishing the necessary separation of duties with existing personnel.

Audit Scope, Objectives, and Methodology

We have conducted a fiscal compliance audit of the Department of Veterans Affairs (DVA) for the period beginning December 8, 2012 and ending March 6, 2016. The audit was conducted 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.

As prescribed by the State Government Article, Section 2-1221 of the Annotated Code of Maryland, the objectives of this audit were to examine DVA's financial transactions, records and internal controls, and to evaluate its compliance with applicable State laws, rules, and regulations.

In planning and conducting our audit, we focused on the major financial-related areas of operations based on assessments of significance and risk. The areas addressed by the audit included procurements and disbursements, cash receipts, federal fund reimbursements, payroll, and property. We also determined the status of the findings contained in our preceding audit report.

Our audit did not include an evaluation of internal controls over compliance with federal laws and regulations for federal financial assistance programs and an assessment of DVA's compliance with those laws and regulations because the State of Maryland engages an independent accounting firm to annually audit such programs administered by State agencies, including DVA.

To accomplish our audit objectives, our audit procedures included inquiries of appropriate personnel, inspections of documents and records, observations of DVA's operations, and tests of transactions. Generally, transactions were selected for testing based on auditor judgment, which primarily considers risk. Unless otherwise specifically indicated, neither statistical nor non-statistical audit sampling was used to select the transactions tested. Therefore, the results of the tests cannot be used to project those results to the entire population from which the test items were selected.

We also performed various data extracts of pertinent information from the State's Financial Management Information System (such as revenue and expenditure data) and the State's Central Payroll Bureau (payroll data), as well as from the contractor administering the State's Corporate Purchasing Card Program (credit card activity). The extracts are performed as part of ongoing internal processes

established by the Office of Legislative Audits and were subject to various tests to determine data reliability. We determined that the data extracted from these various sources were sufficiently reliable for the purposes the data were used during this audit. Finally, we performed other auditing procedures that we considered necessary to achieve our audit objectives. The reliability of data used in this report for background or informational purposes was not assessed.

DVA's management is responsible for establishing and maintaining effective internal control. Internal control is a process designed to provide reasonable assurance that objectives pertaining to the reliability of financial records, effectiveness and efficiency of operations including safeguarding of assets, and compliance with applicable laws, rules, and regulations are achieved.

Because of inherent limitations in internal control, errors or fraud may nevertheless occur and not be detected. Also, projections of any evaluation of internal control to future periods are subject to the risk that conditions may change or compliance with policies and procedures may deteriorate.

Our reports are designed to assist the Maryland General Assembly in exercising its legislative oversight function and to provide constructive recommendations for improving State operations. As a result, our reports generally do not address activities we reviewed that are functioning properly.

This report includes findings relating to conditions that we consider to be significant deficiencies in the design or operation of internal control that could adversely affect DVA's ability to maintain reliable financial records, operate effectively and efficiently and/or comply with applicable laws, rules, and regulations. Our report also includes findings regarding significant instances of noncompliance with applicable laws, rules, or regulations. Other less significant findings were communicated to DVA that did not warrant inclusion in this report.

DVA's response to our findings and recommendations is included as an appendix to this report. As prescribed in the State Government Article, Section 2-1224 of the Annotated Code of Maryland, we will advise DVA regarding the results of our review of its response.

APPENDIX



Maryland Department of Veterans Affairs

Office of the Secretary

LARRY HOGAN
GOVERNOR

BOYD K. RUTHERFORD
LT. GOVERNOR

GEORGE W. OWINGS III
SECRETARY

November 28, 2016

Thomas J. Barnickel III, CPA
Department of Legislative Services
Office of Legislative Audits
301 W. Preston Street, Room 1202
Baltimore, MD 21201

Dear Mr. Barnickel:

I am submitting herewith the response of the Maryland Department of Veterans Affairs (Veterans Affairs) to the recommendations made in the draft audit report on Veterans Affairs for the period beginning December 8, 2012, and ending March 6, 2016. Each individual response is cross-referenced to the respective finding and recommendation from the draft audit report.

Sincerely,

A handwritten signature in black ink, appearing to read "G. Owings III".

George W. Owings III
Secretary

Finding 1

a. Veterans Affairs concurs with the recommendation and has been in compliance for the past two years, since the FY 2014 fiscal closeout. The finding related primarily to FY 2014, a year of leadership transition in the Veterans Affairs fiscal unit.

b. Veterans Affairs concurs with the recommendation and is already in compliance. None of the revenue was ever spent; all has been reverted.

Finding 2

Veterans Affairs concurs with the recommendation and is already in compliance. The expenditures creating the deficit balances occurred over a decade ago, and the resulting deficit was fully eliminated as a result of a deficiency appropriation approved by the Legislature in 2016.

Finding 3

a. Veterans Affairs concurs with the recommendation and has already substantially improved the timeliness of submission of allowance requests to the U.S. Department of Veterans Affairs.

b. Veterans Affairs concurs with the recommendation and is already in compliance. Veterans Affairs' efforts, and those of new U.S. Department of Veterans Affairs fiscal leadership in Baltimore, have resulted in much of the past due balance having been settled since May 2016. The U.S. Department of Veterans Affairs has been remitting payment at an accelerated pace in an effort to resolve the backlog.

Finding 4

a. Veterans Affairs concurs with the recommendation and notes the progress in compliance with State procurement guidelines since hiring its first-ever procurement officer in 2015. Still, existing staffing and resource levels, and the geographical dispersion of Veterans Affairs staff across the State, present significant obstacles to full and timely compliance. Veterans Affairs will seek to achieve substantial compliance with the recommendation by the end of FY 2018.

b. Veterans Affairs concurs with the recommendation and has already implemented processes to document receipt of goods and services prior to payment. Veterans Affairs will continue to take steps necessary to achieve full compliance by the end of FY 2017.

Finding 5

Veterans Affairs concurs with the recommendation. Veterans Affairs notes that the intent of the contract provision permitting a reduction in payment for unfilled

positions was to discourage the contractor from intentionally holding positions vacant; and the contractor has not done so. Veterans Affairs also notes that, as of the date of agency response to Finding 5, the current contract is only weeks from expiration. Prior to close out of the current contract, and not later than March 31, 2017, Veterans Affairs will conduct a review of required staffing information from the contractor and will, to the extent reasonably possible, (a) determine if vacancies of greater than 45 days existed in the absence of extenuating circumstances, and (b) seek to recover the portion of payments made to the contractor related to such vacancies.

Finding 6

a. Veterans Affairs concurs with recommendation and is already in compliance. All collections are recorded immediately upon receipt in both a receipt log and in the State's accounting system.

b. Veterans Affairs concurs with recommendation and is currently performing documented verifications that collections initially recorded are subsequently deposited.

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