

Special Report

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**Statewide Review of  
Budget Closeout Transactions for  
Fiscal Year 2015**

February 2016

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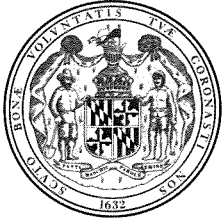
**OFFICE OF LEGISLATIVE AUDITS**  
DEPARTMENT OF LEGISLATIVE SERVICES  
MARYLAND GENERAL ASSEMBLY

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February 2, 2016

Senator Guy J. Guzzone, Co-Chair, Joint Audit Committee  
Delegate Craig J. Zucker, 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, 2015. 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  
Department of Juvenile Services  
Department of State Police  
Department of Veterans Affairs

Additionally, we noted other significant liabilities at June 30, 2015 pertaining to the following agencies.

Maryland State Department of Education  
Department of Health and Mental Hygiene

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

Generally, the non-compliant transactions we identified suggest that additional State funds may be required to eliminate potential deficits. For example, two State agencies recorded federal fund revenues totaling \$3.9 million which could not be substantiated. General fund appropriations (or deficiency appropriations) will be needed to eliminate the resulting deficits if other fund revenues are not available. Similar conditions were noted for both of these agencies in our prior report on the review of fiscal year 2014 closeout transactions.

Another agency inappropriately recorded encumbrances totaling \$9.7 million to avoid cancelling unspent general fund appropriations. Furthermore, one agency did not maintain adequate records to justify retaining special fund balances totaling \$5.4 million at the close of fiscal year 2015 rather than reverting the funds to the General Fund.

Our review noted five state agencies had reported a total of \$60.4 million in unprovided for payables or other liabilities as of June 30, 2015 (Exhibit 2). The expenditures related to these liabilities may have to be funded with subsequent year appropriations (or through a deficiency appropriation). For example, two agencies had reported significant liabilities at June 30, 2015. One agency reported a federal liability of approximately \$30.7 million attributable to the disallowance of certain claims by the federal government. The other agency reported unprovided for general fund payables (that is, accounts payable for which there was a lack of available appropriation) of \$11.9 million. Similar conditions were reported in our report on the review of the fiscal year 2014 closeout transactions related to these two agencies. According to an opinion of the Attorney General, unprovided for payables are 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 objective 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 and to highlight other liabilities that existed at fiscal year-end. 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, appearing to read "TJ Barnickel III".

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 closeout 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 15, 2015, applicable to the fiscal year ended June 30, 2015, the firm stated that the State's financial statements presented fairly, in all material respects, the respective financial position of the State of Maryland as of June 30, 2015, and the respective changes in the financial position and cash flows, for the year then ended in accordance 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 \$321.3 million as of June 30, 2015. This represents an increase of approximately \$173.7 million from the balance reported at the preceding fiscal year-end (\$147.6 million). The *CAFR* also states that the State Reserve (Revenue Stabilization Account) balance totaled \$779.9 million as of June 30, 2015.

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 unencumbered budgetary General Fund balance of \$321.3 million. For example, two GAAP adjustments reduced the Fund balance by \$1.0 billion for income tax collections that are owed to local jurisdictions as June 30, 2015. These adjustments were a total of \$407.9 million smaller than a similar adjustment made for the fiscal year 2014 *CAFR*. Other GAAP adjustments totaling \$60.4 million were made for liabilities incurred by State agencies during fiscal year 2015 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, 2015. 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, 2015, were properly supported and made in accordance with State budgetary laws, regulations, and accounting policies and to determine if other significant liabilities existed at fiscal year-end.

Our review consisted of tests of significant year-end transactions for 20 Departments and independent agencies to ascertain if the transactions were properly supported and made in accordance with State budgetary laws, regulations, and accounting policies and to determine if other significant liabilities existed at fiscal year-end. We reviewed, on a limited basis, transactions processed subsequent to June 30, 2015 to determine if the transactions were properly recorded (such as charged or credited to the proper fiscal year).

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 five issues (appearing in three findings) identified in our January 28, 2015 report entitled *Statewide Review of Budget Closeout Transactions for Fiscal Year 2014*. We determined that four of the five 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 2015 to January 2016.



# **Findings**

## **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 four 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. Additionally, we determined that two departments had other significant liabilities at June 30, 2015 which may require general funds.

## **Revenue Transactions**

Two agencies recorded unsubstantiated revenues to offset federal fund deficits. Specifically, the agencies recorded federal fund revenues totaling approximately \$6.3 million to cover expenditures even though the agencies could not document that these funds would be received. To the extent these funds are not received, general funds will likely be required to eliminate the deficits resulting from these transactions. Similar issues were noted for these two agencies in our fiscal year 2014 closeout review.

## **Expenditure Transactions**

One State agency inappropriately recorded encumbrances totaling \$9.7 million at fiscal year-end to avoid cancelling unspent general fund appropriations.

## **Special Funds**

One State agency could not adequately demonstrate that it was entitled to retain all special funds in one account which totaled \$5.4 million at fiscal year-end rather than reverting the funds to the General Fund.

## **Other Liabilities**

Five state agencies reported a total of \$60.4 million in unprovided for payables or other liabilities as of June 30, 2015. For example, two agencies, which both had similar issues in our fiscal year 2014 closeout report, may require general funds totaling \$42.6 million. One of these agencies has an unfunded federal liability of approximately \$30.7 million attributable to the disallowance of certain claims. The other agency had unprovided for general fund payables of \$11.9 million (that is, accounts payable for which there was a lack of available appropriation). According to an opinion of the Attorney General, unprovided for payables are 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.

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

## Revenue Transactions

### **Finding 1**

**The recovery of recorded federal fund revenues totaling approximately \$6.3 million is uncertain.**

### **Analysis**

The **Department of Veterans Affairs (DVA)** and the **Department of Aging (DOA)** could not substantiate their ability to collect revenues of approximately \$3.4 million and \$2.9 million, respectively, as of June 30, 2015. If these agencies are unable to recover these funds, general funds may be needed to eliminate the resulting deficits.

### DVA

DVA could not provide any documentation supporting federal fund revenues totaling approximately \$1.0 million would be received. This federal fund revenue was recorded at year end to eliminate deficit balances. According to the Comptroller of Maryland – General Accounting Division (GAD), these deficits resulted from federal fund expenditures incurred during prior years. This issue has been commented upon in our four preceding budgetary closeout reports.

Furthermore, DVA has recorded federal fund revenue to cover expenditures related to the burial of veterans. However, DVA has experienced significant delays in being reimbursed by the federal government for payments related to these burials. Because of the length of the reimbursement delays, we question whether all of the amounts outstanding will be received. As of January 11, 2016, DVA had not been reimbursed approximately \$830,000 for fiscal year 2014 burials and \$1.57 million for fiscal year 2015. According to DVA management, it is in the process of working with the U.S. Department of Veterans Affairs to improve the reimbursement process.

### DOA

DOA recorded federal fund revenue transactions of approximately \$2.9 million at June 30, 2015. These revenue transactions related to federal fund expenditures for the Medicaid Waiver grant that were incurred during fiscal year 2015 and prior years. However, as of January 12, 2016 requests for reimbursement of these expenditures had not been prepared. This issue has been commented upon in our three preceding budgetary closeout reports.

## Expenditure Transactions

### **Finding 2**

**Unexpended general fund appropriations totaling approximately \$9.7 million were not cancelled at fiscal year-end.**

### **Analysis**

The **Department of Juvenile Services (DJS)** inappropriately recorded encumbrances to avoid cancelling unspent general fund appropriations totaling approximately \$9.7 million. This practice violated the yearly closing instructions of the Comptroller of Maryland - General Accounting Division (GAD) since the encumbrances did not represent actual fiscal year-end commitments by the State for goods and services and consequently would not qualify as valid encumbrances. As of June 30, 2015, DJS did not have any obligations, such as approved contracts, to support the encumbrance of these appropriations. Consequently, the encumbrances should not have been recorded and the related appropriations should have been cancelled so that the funds could revert to the General Fund.

## Special Funds

### **Finding 3**

**One agency did not maintain adequate records to justify retaining \$5.4 million in special funds.**

### **Analysis**

The **Maryland Department of State Police (DSP)** retained special funds totaling \$5.4 million related to field operations without maintaining adequate records to document the legal authority to retain the funds. Under this appropriation, DSP accounted for billed external services provided under several of its programs including Automotive Safety Enforcement Division, Commercial Vehicle Enforcement Division, Reimbursable Overtime, John F. Kennedy Memorial Highway, Resident Trooper, and Speed Camera Monitoring. Our fiscal compliance audit report dated November 23, 2015, disclosed DSP did not account for financial activity for each of these programs separately. As a result, the specific fund balances for each of these programs were unavailable and, we were unable to determine if specific legal justification existed for DSP to retain all of the special funds remaining at fiscal year-end rather than reverting the funds to the General Fund.

## Other Liabilities

### Finding 4

**Five agencies reported a total of \$60.4 million in unprovided for payables or other liabilities as of June 30, 2015.**

### Analysis

Five agencies had a total of \$60.4 million in unprovided for payables or other liabilities as of June 30, 2015 (see Exhibit 2). The expenditures related to these liabilities may have to be funded with subsequent year appropriations (or through a deficiency appropriation). For example, one agency reported a federal liability of approximately \$30.7 million attributable to the disallowance of certain claims while another agency reported unprovided for general fund payables of \$11.9 million (that is, accounts payable for which there was a lack of available appropriation). According to an opinion of the Attorney General, unprovided for payables are 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.

### DHMH

The **Department of Health and Mental Hygiene (DHMH)** has a liability to the federal government of approximately \$34.1 million for disallowed claims related to **Developmental Disabilities Administration (DDA)** residential add-on services. During the closeout process, DDA recorded expenditures of \$3.4 million to repay a portion of the disallowed claims using general funds. Funding sources for the remaining liability of \$30.7 have not been identified. DHMH reported the potential liability to GAD and, GAD recorded a decrease to the General Fund in the State's fiscal year 2015 *Comprehensive Annual Financial Report* to recognize these disallowances. The claims were disallowed by the federal Department of Health and Human Services – Office of the Inspector General in its June 2015 audit report which recommended that DDA refund the overbilled amount to the federal government. DDA is disputing the disallowed claims. Disallowed federal fund claims were also commented upon in our preceding budgetary closeout report.

### MSDE

The **Maryland State Department of Education (MSDE)** has a liability in fiscal year 2015 to local education agencies of approximately \$11.9 million for nonpublic placements in its Students with Disabilities – Aid to Education program. Specifically, MSDE fiscal year 2015 general fund expenditures for nonpublic placements in its Students with Disabilities – Aid to Education program totaled \$123.2 million while the related appropriation was only \$110.9 million,

resulting in a deficit of \$12.3 million. MSDE was able to reduce this deficit to \$11.9 million using \$400,000 in excess funds provided in a fiscal year 2015 deficiency appropriation totaling \$10.8 million related to excess fiscal year 2014 expenditures. MSDE reported the liability to GAD and, GAD recorded a decrease to the General Fund in the State's fiscal year 2015 *Comprehensive Annual Financial Report* to recognize this deficit. A similar situation regarding unfunded liabilities in this program was commented on in our preceding budgetary closeout report.

## **Exhibit 1**

### **Summary of Fiscal Year 2015 Closeout Review Findings by State Agency**

<b>Agency</b>	<b>Finding Number</b>	<b>Finding Description</b>
<b>Department of Veterans Affairs</b>	<b>1*</b>	Recovery of \$3.4 million in recorded federal fund revenues is uncertain
<b>Department of Aging</b>	<b>1*</b>	\$2.9 million in federal fund revenues were recorded even though related federal funds may not be available
<b>Department of Juvenile Services</b>	<b>2</b>	Unexpended general fund appropriations totaling \$9.7 million were not cancelled at fiscal year-end
<b>Maryland Department of State Police</b>	<b>3</b>	Adequate special funds records were not maintained to justify retention of funds totaling \$5.4 million at fiscal year-end
<b>Department of Health and Mental Hygiene</b>	<b>4*</b>	A federal liability of approximately \$30.7 million may have to be funded with State general funds
<b>Maryland State Department of Education</b>	<b>4*</b>	Unprovided for general fund payables of \$11.9 million existed

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



## Exhibit 2

### Schedule of June 30, 2015 Unprovided for General Fund Payables and Other Liabilities Reported to the General Accounting Division

Agency	Amount of Reported Unprovided for Payables / Other Liabilities As of June 30, 2015
Department of Health and Mental Hygiene	\$30,723,848
Maryland State Department of Education	12,410,913
Maryland Higher Education Commission	6,791,494
Department of State Police	5,574,944
Office of the Public Defender	4,894,813
<b>Total</b>	<b>\$60,396,012</b>

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