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**OFFICE OF  
THE INSPECTOR GENERAL**

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**SOCIAL SECURITY ADMINISTRATION**

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**SINGLE AUDIT OF THE  
STATE OF WASHINGTON  
FOR THE FISCAL YEAR ENDED  
JUNE 30, 2005**

**January 2007                  A-77-07-00006**

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**MANAGEMENT  
ADVISORY REPORT**

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## **Mission**

**By conducting independent and objective audits, evaluations and investigations, we inspire public confidence in the integrity and security of SSA's programs and operations and protect them against fraud, waste and abuse. We provide timely, useful and reliable information and advice to Administration officials, Congress and the public.**

## **Authority**

**The Inspector General Act created independent audit and investigative units, called the Office of Inspector General (OIG). The mission of the OIG, as spelled out in the Act, is to:**

- Conduct and supervise independent and objective audits and investigations relating to agency programs and operations.**
- Promote economy, effectiveness, and efficiency within the agency.**
- Prevent and detect fraud, waste, and abuse in agency programs and operations.**
- Review and make recommendations regarding existing and proposed legislation and regulations relating to agency programs and operations.**
- Keep the agency head and the Congress fully and currently informed of problems in agency programs and operations.**

**To ensure objectivity, the IG Act empowers the IG with:**

- Independence to determine what reviews to perform.**
- Access to all information necessary for the reviews.**
- Authority to publish findings and recommendations based on the reviews.**

## **Vision**

**We strive for continual improvement in SSA's programs, operations and management by proactively seeking new ways to prevent and deter fraud, waste and abuse. We commit to integrity and excellence by supporting an environment that provides a valuable public service while encouraging employee development and retention and fostering diversity and innovation.**



## SOCIAL SECURITY

### **MEMORANDUM**

Date: January 18, 2007

Refer To:

To: Candace Skurnik  
Director  
Audit Management and Liaison Staff

From: Inspector General

Subject: Management Advisory Report: Single Audit of the State of Washington for the Fiscal Year Ended June 30, 2005 (A-77-07-00006)

This report presents the Social Security Administration's (SSA) portion of the single audit of the State of Washington for the Fiscal Year ended June 30, 2005. Our objective was to report internal control weaknesses, noncompliance issues, and unallowable costs identified in the single audit to SSA for resolution action.

The Washington State Auditor performed the audit. The Department of Health and Human Services (HHS) desk review concluded that the audit met Federal requirements. In reporting the results of the single audit, we relied entirely on the internal control and compliance work performed by the State Auditor and the reviews performed by HHS. We conducted our review in accordance with the *Quality Standards for Inspections* issued by the President's Council on Integrity and Efficiency.

For single audit purposes, the Office of Management and Budget assigns Federal programs a Catalog of Federal Domestic Assistance (CFDA) number. SSA's Disability Insurance (DI) and Supplemental Security Income (SSI) programs are identified by CFDA number 96. SSA is responsible for resolving single audit findings reported under this CFDA number.

The Washington Disability Determination Services (DDS) performs disability determinations under SSA's DI and SSI programs in accordance with Federal regulations. The DDS is reimbursed for 100 percent of allowable costs. The Washington Department of Social and Health Services (DSS) is the Washington DDS' parent agency.

The single audit reported that:

1. The DDS did not comply with State and Federal contract procurement regulations when purchasing consultative evaluations (CE). (Attachment A, pages 1 through 5). The corrective action plan indicated that CE services will be competitively procured in the future. (Attachment A, page 6).
2. DDS expenditures were not accurately reported on the Schedule of Expenditures of Federal Awards and the quarterly report of obligations. (Attachment A, pages 7 through 9). The corrective action plan indicated that a reconciliation method will be implemented to ensure that the disbursement amounts reported to SSA reconcile to the State accounting system. (Attachment A, page 10).
3. Unallowable indirect costs totaling \$19,555 were charged to SSA for the Cooperative Disability Investigations Unit (CDIU). The Memorandum of Understanding, which identified specific costs allowed for reimbursement, did not include a provision for indirect costs. The unallowable costs could be even higher if this condition occurred in the other quarters. (Attachment A, pages 11, 12, and 13). The corrective action plan indicated that the DDS is working with SSA to revise the Memorandum of Understanding to include a provision for indirect costs. (Attachment A, page 14).
4. The DDS claimed reimbursement for \$56,466 for costs that were not supported by documentation. The unallowable costs could be even higher if this condition occurred in the other quarters. (Attachment A, pages 11, 12, and 13). The DDS has implemented internal controls to ensure expenditures are supported by adequate documentation prior to payment. (Attachment A, page 14).

We recommend SSA:

1. Work with the DDS to ensure CE services are purchased in accordance with State and Federal regulations.
2. Verify that controls are in place to ensure that expenditures are accurately reported on all Federal and State reports.
3. Determine the total indirect costs that have been charged to SSA for the CDIU since its inception and collect the unallowable costs.
4. Determine if the \$56,466 that was not supported by documentation are allowable charges and collect any unallowable costs.
5. Ensure the DDS has procedures in place to maintain documentation to support expenditures charged to its program.

Page 3 – Candace Skurnik

The single audit also disclosed that computer access controls were not in place to ensure there is adequate separation of duties for personnel in the accounting department (Attachment B, pages 1, 2 and 3). Although this finding was not specifically identified to SSA it may have an impact on DDS operations. I am bringing this matter to your attention as it represents a potential serious service delivery and financial control problem for the Agency.

Please send copies of the final Audit Clearance Document to Shannon Agee and Rona Lawson. If you have any questions contact Shannon Agee at (816) 936-5590.

A handwritten signature in black ink, appearing to read "Patrick P. O'Carroll, Jr."

Patrick P. O'Carroll, Jr.

Attachments

05-39      **The Department of Social and Health Services, Division of Disability Determination Services, did not comply with state and federal regulations when contracting for services paid with Social Security Disability Insurance Program funds.**

#### **Background**

The Department of Social and Health Services, Division of Disability Determination Services, administers the Social Security Disability Insurance Program (CFDA 96.001) with funds from the U.S. Social Security Administration. This Program pays monthly cash benefits to eligible claimants to replace earnings lost due to physical or mental impairments that prevent the individual from working. In general, State agencies make initial disability determinations for the federal government, which then pays them, either in advance or in reimbursement, for the costs of making such determinations. During fiscal year 2005, the Division spent \$37,582,178 in federal funds to determine claimants' medical eligibility for disability benefits.

To assist in making proper determinations, the Division purchases medical examinations, X-ray services and laboratory tests to supplement evidence obtained from the claimants' physicians or other health care sources. These purchases are for personal services known as consultative evaluations and are obtained from two sources: individual medical professionals and companies that employ or subcontract with medical professionals. In state fiscal year 2005, the Division spent \$5,225,989 for consultative evaluations by individual medical practitioners and \$2,514,388 for consultative evaluations by companies that employ or subcontract with medical professionals.

Federal regulations applicable to the awarding of federal funds to states require the states to follow their own laws and regulations for contracting for services with these funds. Personal service contracts in this state must follow prescribed procurement regulations, including a formal competitive procurement process if the amount is more than \$20,000.

#### **Description of Condition**

The Division did not comply with state regulations for contract procurement and therefore is not in compliance with federal regulations. During our review, we found:

- For consultative evaluations by individual medical practitioners:
  - No competitive procurement process was followed for these services. The Division learned of interested providers informally through word-of-mouth. Many practitioners were paid amounts that substantially exceeded the threshold of \$20,000, requiring a formal competitive procurement process.
  - No contracts existed for any of these services.
- For consultative evaluations by companies that employ or subcontract with medical professionals:
  - The Division mailed a solicitation letter to four companies without establishing whether other companies might be interested in competing for the business. The Division did not have written documentation explaining why more firms were not contacted.
  - Of the four companies contacted, two responded. Division management stated that the other companies did not submit proposals because of insurance requirements. This is of particular concern because, after we discovered and reported to management that one of the two contractors did not meet the insurance requirements, the Division granted an exception from this requirement to the contractor. Since insurance was part of the contract procurement requirements, granting an exception may not have been in the best interests of the state.

#### **Cause of Condition**

The condition was caused by lack of knowledge regarding state procurement requirements.

#### **Effect of Condition**

The Department cannot ensure the state's resources were used in the most economical manner possible. In addition, the state may not be adequately protected when more than \$5 million in services is purchased without written contracts and terms.

We question the \$7,740,327 in federal funds paid for both types of consultative evaluation services in fiscal year 2005.

#### **Recommendation**

We recommend the Department:

- Properly classify consultative evaluation contracts as personal service contracts.
- Follow appropriate competitive procurement procedures.
- Prepare and maintain contract documentation for consultative evaluations by individual medical practitioner.

#### **Department's Response**

*The Department of Social and Health Services, Division of Disability Determination Services (DDDS) does not agree with the auditor's assertion that medical providers who perform consultative examinations of claimants should be categorized as personal services and therefore these services must be competitively procured. The Division has been operating under the Office of Financial Management (OFM) classification of these contracts as client service. We recognize that there is a difference of opinion between the auditors and OFM. The Division will seek clarification of whether these services should be classified as personal service or client service from OFM.*

*Per our federal guidelines contained in the Social Security Administration's (SSA) Program Operational Manual Systems (POMS), DI 39545.260 #8, "The Division may consider conducting a study to determine the feasibility of using competitively awarded contracts for medical services with both large and small volume providers, including individual and group practices."*

*The Division would like to correct the auditor's statement that "after we discovered and reported to management that one of the two contractors did not meet the insurance requirement; the Division granted an exception from this requirement to the contractor. Since insurance was part of the contract procurement requirements, granting an exception may not have been in the best interests of the state."*

*This contractor was a limited liability company (LLC) formed by a non-medical individual who had two psychiatrists who worked for the business entity. These medical providers perform the Division's medical evaluations. While the business entity was able to acquire liability insurance in the amounts the Department requires, the business entity could not acquire medical liability or omissions insurance. However, the two medical providers who worked for the entity each had the appropriate medical liability insurance in the amounts required by the Department and submitted certificates of insurance proving this to Central Contracting Services (CCS). CCS is the Department's contracting authority and CCS accepted the insurance coverage as it pertained to this entity as meeting the Department's contractor insurance requirement. The insurance requirement was not waived for this entity.*

*The Division agrees with the auditor's finding that no contracts exist with individual medical providers. The Division is given the responsibility of management and oversight of the Consultative Examination Process. One of the Policy Guidelines the Division must follow is to, "Maintain a good working relationship with the medical community in order to recruit sufficient physicians and other providers of medical services to ensure ready availability of Consultative Examination providers." (POMS DI 29545.230) On average, the Division sends 100-150 recruiting letters a year to professionals requesting their services in areas throughout the state. Our typical success rate is between 10-20%. The Division has difficulty recruiting because:*

- SSA documentation and report requirements are detailed and very specific
- Examinations take a considerable amount of time out of a doctor's practice
- Our client population has a risk of not showing for appointments which adds more burden of lost time and money for professionals
- DDDS fees are not commensurate with market rate for the detail we require
- Because of the malpractice insurance cost and doctors leaving WA state to practice elsewhere, resources are depleted, especially in rural areas and professionals are too busy with their own patients
- Specialists are already too busy with their own patients and do not have the necessary time to spend to do an exam and report
- Health Maintenance Organization's, Health Networks, etc. do not allow doctors to "moonlight" or work outside their company

The Division has always used a fee for service voucher contract for individual doctors because of the difficulty we have in recruiting. As long as professionals meet the professional qualifications for doing consultative exams, we do not turn anyone away. We supply them with our rules, regulations, and guidelines and put them in the mix of scheduling. Our scheduling system is designed to create a fair and equitable process. Examination requests are pulled up on a queue based, on location of claimant, and type of exam. Corresponding available doctors meeting this criterion come up for scheduling. Doctors appear for scheduling in a rotational order. After an exam is scheduled with a doctor, he/she then moves to the bottom of the list and will not be scheduled again until we have scheduled with all other available, willing, and eligible doctors. In some areas, we may only have one doctor available and willing.

Due to the large number of psychiatric examinations (60 percent of our exams), and the lack of psychiatrists willing to do these examinations, we developed client service contracts to appeal to a provider or company by offering volume of exams in different counties. In an effort to ensure the state's resources were used economically and still obtain the necessary service, we set the client service contract fee lower than our published fee schedule. Even though client service contracts do not require a competitive bid process, we did send the contracts to five companies and one individual provider. One company did not respond, two responded stating our fees were too low, and the individual provider could not meet the insurance requirements. Of the two companies that bid the contract, both were awarded.

Because of the reasons associated with difficulty in recruiting, we often will attract semi-retired or retired providers who may not carry the amount of insurance required by Department contracts. The Division examinations are a one time medical or mental assessment of the claimant which considerably reduces the risk to the provider and the Department. Because of the extremely low risk to the state, the Division does not require the Department's insurance required amount, in order to maintain a sufficient amount of resources as directed by SSA.

The Division is in the process of drafting a Core Provider Agreement similar to those used by the Health and Recovery Services Administration/Medical Assistance Administration for all independent providers. We are working with the Attorney General's office to develop the appropriate language for the agreement and hope to have this ready for dissemination by the end of the calendar year.

#### Auditor's Concluding Remarks

We considered the Division's response and reaffirm our finding.

We relied on the Office of Financial Management contract guidelines to help determine if these contracts should properly be considered personal services contracts. Based on grant documentation, the federal government refers the disabled worker to the Division to assist it in making a disability determination and reimburses the Division for its costs; therefore, the federal government, not the applicant, is the Division's client.

Division management stated it was difficult to recruit providers for these services but did not provide evidence of a recruiting and evaluation process to support that statement. In addition, we remain concerned about the lack of contract documentation of insurance coverage that was part of the application requirement.

We appreciate the Department's efforts to resolve the issues identified in the finding and we will review the corrective action in the fiscal year 2006 audit. We also appreciate the cooperation extended to us throughout the audit by Department staff.

**Applicable Laws and Regulations**

The U.S. Office of Management and Budget's *Cost Principles for State, Local and Indian Tribal Governments*, Circular A-87, Attachment A, Section C states in part:

1. Factors affecting allowability of costs. To be allowable under Federal awards, costs must meet the following general criteria:
  - c. Be authorized or not prohibited under State or local laws or regulations...

RCW 39.29.006 states in part:

(3) "Competitive solicitation" means a documented formal process providing an equal and open opportunity to qualified parties and culminating in a selection based on criteria which may include such factors as the consultant's fees or costs, ability, capacity, experience, reputation, responsiveness to time limitations, responsiveness to solicitation requirements, quality of previous performance, and compliance with statutes and rules relating to contracts or services.

(7) "Personal service" means professional or technical expertise provided by a consultant to accomplish a specific study, project, task, or other work statement....

RCW 39.29.011 states in part:

All personal service contracts shall be entered into pursuant to competitive solicitations, except for...

- (1) Emergency contracts;
- (2) Sole source contracts;
- (3) Contract amendments;

(4) Contracts between a consultant and an agency of less than twenty thousand dollars. However, contracts of five thousand dollars or greater but less than twenty thousand dollars shall have documented evidence of competition. Agencies shall not structure contracts to evade these requirements;...

The Office of Financial Management's *State Administrative and Accounting Manual*, states in Section 15.10.10:

Personal services are to be procured and awarded by state agencies in accordance with the requirements of Chapter 39.29 RCW.

Section 15.20.30.a states:

Competitive solicitation for contracts of \$20,000 or greater requires a documented, formal solicitation process as described in the following subsections. (*Auditor's note: Following this section are detailed regulations for this process.*)

Section 20.20.20 states in part:

Each agency director is responsible for establishing and maintaining an effective system of internal control throughout the agency.

The Office of Financial Management's *Guide to Personal Service Contracting*, Section 1.3, states in part:

Personal services are professional or technical services provided by a consultant to accomplish a specific study, project, task, or other work statement. Consultants, who provide personal services, serve state agencies as objective advisers by rendering professional opinions, judgments, or recommendations.

Section 1.6 of the *Guide* lists as an example of personal services:

Medical and psychological services, including evaluation and consultative services

The Office of Financial Management's *Guide to Client Service Contracting*, Introduction, page 2, states in part:

Clients are those individuals the agency has statutory responsibility to serve, protect, or oversee..

**State of Washington  
Corrective Action Plan**

***OMB Circular A-133 Audit  
For the Fiscal Year Ended  
June 30, 2005***

(This plan only addresses findings reportable under the revised OMB Circular A-133.)

**Department of Social and Health Services (DSHS)**

<b>Fiscal Year</b>	<b>Finding Number</b>	<b>Finding and Corrective Action Plan</b>					
05	39	<p>Finding:</p> <p>The Department of Social and Health Services, Division of Disability Determination Services, did not comply with state and federal regulations when contracting for services paid with Social Security Disability Insurance Program funds.</p> <p>Questioned Costs:</p> <table><thead><tr><th><u>CFDA #</u></th><th><u>Amount</u></th></tr></thead><tbody><tr><td>96.001</td><td>\$7,740,327</td></tr></tbody></table> <p>Status:</p> <p>Corrective action in progress.</p> <p>Corrective Action:</p> <p>The Division has consulted with the Office of Financial Management (OFM) regarding the proper classification for our consultative evaluation services. OFM determined that services provided to our claimants by physicians, psychologists and psychiatrists are in fact, personal services.</p> <p>The Division will develop and issue a personal service contract to any medical provider who agrees to see our claimants at our fee schedule. The Division will monitor the competitive procurement process for any decrease in the number of providers available to perform evaluations.</p> <p>Based on OFM's determination, the Division will competitively procure for consultative examination services. The Division will issue personal service contracts for any individual medical practitioner.</p> <p>Completion Date:</p> <p>Estimated, October 2007</p>	<u>CFDA #</u>	<u>Amount</u>	96.001	\$7,740,327	
<u>CFDA #</u>	<u>Amount</u>						
96.001	\$7,740,327						

05-40      The Department of Social and Health Services, Division of Disability Determination Services, reported incorrect expenditures for the Social Security Disability Insurance Program on several reports, including the Schedule of Expenditures of Federal Awards.

#### **Background**

The Department of Social and Health Services, Division of Disability Determination Services, administers the Social Security Disability Insurance Program (CFDA 96.001) with funds from the U.S. Social Security Administration. This Program pays monthly cash benefits to eligible claimants to replace earnings lost due to physical or mental conditions that prevent the individual from working. In general, State agencies make initial disability determinations for the federal government, which then pays them, either in advance or through reimbursement, for the costs of making such determinations. During fiscal year 2005, the Division spent \$37,582,178 in federal funds to determine claimants' medical eligibility for disability benefits.

As part of monitoring the Division and its performance, the Social Security Administration requires specific reports to be filed weekly, monthly, quarterly, and annually. The quarterly Report of Obligations for SSA Disability Programs helps the Administration to plan and authorize federal funding for the Division. In addition, as a condition of receiving federal funds, state agencies must report the total spent during the state fiscal year on the annual Schedule of Expenditures of Federal Awards.

#### **Description of Condition**

When we attempted to reconcile reported Program data to accounting records, we found::

- The amount reported in the Schedule of Expenditures of Federal Awards was overstated by \$2,218,301. June medical accruals, which are liabilities that have not been paid by the Division, were mistakenly entered twice into the state's Agency Financial Reporting System at fiscal year end.
- The yearly total of the payment amounts taken from the Division's in-house accounting system and reported in the quarterly Reports of Obligations was understated by \$1,203,997. Division management had no explanation for this underreporting.

#### **Cause of Condition**

The Division does not reconcile among its various reports and two different accounting systems to ensure differences are identified, explained and corrected in a timely manner.

#### **Effect of Condition**

The federal grantor has not received accurate information to use for monitoring purposes. This could affect future federal funding.

#### **Recommendations**

We recommend the Division perform adequate reconciliations to ensure it is reporting correct Program financial data to the grantor.

#### **Department's Response**

*The Division agrees with the finding that the Division's June medical accrual journal voucher was entered into the state accounting system twice in error. This breakdown in normal internal control procedures occurred as a direct result of being short staffed, with two of four staff gone on maternity leave. This is an isolated incident that should not occur in the future.*

*The Division along with the Office of Accounting Services (OAS) is attempting to reconcile the Division's Quarterly 4513 reports to the amounts that OAS reports on the Schedule of Expenditures of Federal Awards (SEFA) for state fiscal year 2005. OAS will report the conclusion of the reconciliation to the Auditors as soon as possible. However,*

*it is unknown, due to the complexity of the two different bases used, if a complete reconciliation will be possible. OAS reports grant expenditures on the SEFA with different bases than the Division reports expenditures and obligations to SSA. There is also the question of grant monies reported under the two Catalog of Federal Domestic Assistance (CFDA) numbers that SSA funds roll up to because they include grant funds expended by the Division of Vocational Rehabilitation. These expenditures are not included in the Division's official Quarterly 4513 reports.*

*The Division disagrees with the Auditor's "Cause of Condition." The Division uses the State's Agency Financial Reporting System (AFRS) for all expenditure processing and uses the State's Enterprise Reporting System to pull detailed reports of expenditures. The Division's in-house system, AS400, is used to collect medical obligation data only. The Division has internal controls in place to ensure all expenditure or disbursement data and all known obligations are reported to SSA in the period that they occur.*

#### Auditor's Concluding Remarks

The Department was not able to provide us with appropriate reconciliations during our review. We reaffirm our finding that Program expenditures were reported incorrectly.

We appreciate the Department's commitment to resolving the issues identified in the finding and will review the corrective action in the fiscal year 2006 audit. We also appreciate the cooperation extended to us throughout the audit by Department staff.

#### Applicable Laws and Regulations

The U. S. Office of Management and Budget's Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, Subpart C, states in part:

##### Section .310 Auditee Responsibilities: Financial Statements

- (b) Schedule of expenditures of Federal awards. The auditee shall also prepare a schedule of expenditures of Federal awards for the period covered by the auditee's financial statements. . . . At a minimum, the schedule shall:
  - (1) List individual Federal programs by Federal agency. For Federal programs included in a cluster of programs, list individual Federal programs within a cluster of programs.
  - (3) Provide total Federal awards expended for each individual Federal program and the CFDA number or other identifying number when the CFDA information is not available.

Title 20 of the Code of Federal Regulations, Part 437, *Uniform Administrative Requirements for Grants and Cooperative Agreements to State and Local Governments*, states in part:

##### Section 437.20 Standards for financial management systems. Financial Administration:

- (a) A State must expend and account for grant funds in accordance with State laws and procedures for expending and accounting for its own funds. Fiscal control and accounting procedures of the State, as well as its subgrantees and cost-type contractors, must be sufficient to—
  - (1) Permit preparation of reports required by this part and the statutes authorizing the grant, and
  - (2) Permit the tracing of funds to a level of expenditures adequate to establish that such funds have not been used in violation of the restrictions and prohibitions of applicable statutes.

- (b) The financial management systems of other grantees and subgrantees must meet the following standards:
- (1) Financial reporting. Accurate, current, and complete disclosure of the financial results of financially assisted activities must be made in accordance with the financial reporting requirements of the grant or subgrant.
  - (2) Accounting records. Grantees and subgrantees must maintain records that adequately identify the source and application of funds provided for financially-assisted activities. These records must contain information pertaining to grant or subgrant awards and authorizations, obligations, unobligated balances, assets, liabilities, outlays or expenditures, and income.
  - (3) Internal control. Effective control and accountability must be maintained for all grant and subgrant cash, real and personal property, and other assets. Grantees and subgrantees must adequately safeguard all such property and must assure that it is used solely for authorized purposes.

The Office of Financial Management's *State Administrative and Accounting Manual* lists the following accounting and control requirements:

**Section 50.30.45:**

**Responsibilities of state agencies/institutions administering or expending federal awards**

1. Develop internal policies in accordance with this policy and the requirements of the Act and Circular.
2. Identify, account for, and report all expenditures of federal awards in accordance with laws, regulations, contract and grant agreements, and requirements included in this and other sections of the OFM, State Administrative and Accounting manual.
3. Provide year-end, certified, federal financial data per requirements included in Chapter 95.

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**State of Washington  
Corrective Action Plan**

***OMB Circular A-133 Audit  
For the Fiscal Year Ended  
June 30, 2005***

(This plan only addresses findings reportable under the revised OMB Circular A-133.)

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**Department of Social and Health Services (DSHS)**

Fiscal Year	Finding Number	Finding and Corrective Action Plan					
05	40	<p>Finding:</p> <p>The Department of Social and Health Services, Division of Disability Determination Services, reported incorrect expenditures for the Social Security Disability Insurance Program on several reports, including the Schedule of Expenditures of Federal Awards.</p> <p>Questioned Costs:</p> <table><thead><tr><th>CFDA #</th><th>Amount</th></tr></thead><tbody><tr><td>96.001</td><td>\$0</td></tr></tbody></table> <p>Status:</p> <p>Corrective action in progress.</p> <p>Corrective Action:</p> <p>The Division of Disability Determination Services had a temporary breakdown of internal controls when two of four of the administrative accounting staff were out on maternity leave. Since then, the Division has reviewed internal controls to ensure that this type of error will not occur in the future.</p> <p>The Division reports disbursements from the state accounting system and reports obligations from an in-house legacy system. The Division is highly motivated to ensure that the amounts from both systems agree to our official report to the Federal grantor.</p> <p>The Division is in the process of implementing a reconciliation method and other procedures to ensure that the disbursement amounts reported on the 4513 report agree to the state accounting system. This reconciliation is expected to be completed by June 30, 2006.</p> <p>Completion Date:</p> <p>Estimated, June 2006</p>	CFDA #	Amount	96.001	\$0	
CFDA #	Amount						
96.001	\$0						

**05-41      The Department of Social and Health Services, Division of Disability Determination Services, received reimbursement for unallowable costs for the Social Security Disability Insurance Program.**

#### **Background**

The Department of Social and Health Services, Division of Disability Determination Services, administers the Social Security Disability Insurance Program (CFDA 96.001) with funds from the U.S. Social Security Administration. This Program pays monthly cash benefits to eligible claimants to replace earnings lost due to physical or mental impairments that prevent the individual from working. In general, state agencies make initial disability determinations for the federal government, which then pays them, either in advance or in reimbursement, for costs in making such determinations. During fiscal year 2005, the Division spent \$37,582,178 in federal funds to determine claimants' medical eligibility for disability benefits.

Federal regulations require states to follow their own laws and regulations when spending federal funds. The state of Washington requires all expenditures to be adequately supported and has described the minimum standards for payment support.

#### **Description of Condition**

The Division, the Social Security Administration, and the Washington State Patrol entered into a Memorandum of Understanding in October 2004 to create a Cooperative Disability Investigations Unit to investigate cases of possible disability fraud. The agreement names specific allowed costs for the Patrol and states that the Division will reimburse the Patrol only for those costs. The agreement does not include any provision for indirect costs.

We reviewed one 2005 quarterly billing from the Patrol for \$76,021, consisting of \$19,555 for unallowable indirect costs and \$56,466 for other costs that were unallowable because they were not supported by documentation provided by the Patrol. We found the Division paid the total invoice and then requested reimbursement from the Administration.

#### **Cause of Condition**

The Division did not adequately review the transaction and the Memorandum of Understanding prior to payment and request for reimbursement to determine which costs were allowable.

#### **Effect of Condition**

The Division received funds from the federal grantor for payments that were unallowable under Memorandum terms and federal and state regulations. We question the \$76,021 in unallowable costs we found in this one quarterly billing. Unallowable costs could be even higher if other billings had similar conditions.

#### **Recommendations**

We recommend the Division:

- Strengthen its review of documentation before making future payments and requesting reimbursement.
- Review prior billings to determine if it paid other unallowable costs, request reimbursement for any improper amounts from the Patrol, and then reimburse the federal grantor for these amounts.

#### **Department's Response**

*The Department of Social and Health Services, Division of Disability Determination Services agrees with the Auditor's assessment that the Division may have paid indirect costs to the Washington State Patrol (WSP) that would be considered unallowable because there was no provision for these costs in the Memorandum of*

*Understanding (MOU) that was signed by representatives from the Social Security Administration (SSA), the Division and the WSP.*

*The Division has been in contact with SSA's Regional Office in Seattle. This office has federal oversight over the Division and wrote the original MOU between SSA, WSP and the Division. Currently, SSA's Regional Office is writing a new MOU between all parties involved. The new MOU will include a provision for indirect costs.*

*The Division agrees with the Auditor's finding that the Division paid \$56,466 to the WSP that was not supported by adequate back-up documentation. However, the costs in question were payroll costs and these are allowable costs under the terms of the MOU. Since the audit, the Division reviewed all paid WSP billings from the inception of the Cooperative Disability Investigations Unit (January 2003) until current and did not find any instance where the Division over or underpaid the WSP.*

*The Division agrees that Fiscal Staff did not previously completely review the WSP billing documentation adequately. The Division has implemented internal controls that will ensure that every billing is reviewed for adequate documentation prior to payment.*

#### **Auditor's Concluding Remarks**

We appreciate the Department's commitment to resolving the issues identified in the finding and will review the corrective action in the fiscal year 2006 audit. We also appreciate the cooperation extended to us throughout the audit by Department staff.

#### **Applicable Laws and Regulations**

Title 20 of the Code of Federal Regulations, Section 437, *Uniform Administrative Requirements for Grants and Cooperative Agreements to State and Local Governments*, states in part:

##### **437.20 Standards for financial management systems. Financial Administration:**

- (a) A State must expend and account for grant funds in accordance with State laws and procedures for expending and accounting for its own funds.
- (b) The financial management systems of other grantees and subgrantees must meet the following standards:
  - (5) Allowable cost. Applicable OMB cost principles, SSA program regulations, and the terms of grant and subgrant agreements will be followed in determining the reasonableness, allowability, and allocability of costs.
  - (6) Source documentation. Accounting records must be supported by such source documentation as cancelled checks, paid bills, payrolls, time and attendance records, contract and subgrant award documents, etc.

The Office of Financial Management's *State Administrative and Accounting Manual* lists the following accounting and control requirements:

##### **Section 85.32.10: Agency Responsibilities**

It is the responsibility of the agency head, or authorized designee, to certify that all expenditures/expenses and disbursements are proper and correct. Agencies are responsible for processing payments to authorized vendors, contractors, and others providing goods and services to the agency. Agencies are to establish and implement procedures following generally accepted accounting principles.

**Section 85.32.20b: Payment Authorization**

Prior to payment authorization, agencies are to verify that the goods and services received comply with the specifications indicated on the purchase documents. Authorized personnel receiving the goods and services are to indicate the actual quantities received.

**Section 85.32.30a: Payment Processing Documentation**

At a minimum, payment processing documentation should include evidence of authorization for purchase, receipt of goods or services, and approval for payment.

**Section 85.32.40: Payment Processing related to accuracy of support states in part:**

- (b) Agencies are to establish procedures which verify the mathematical accuracy of all documents and ensure that charges are properly recorded to the appropriate accounts.
- (c) Audit disbursement documents for the following:
  - Quantities indicated on the invoice agree with those documented as received on the receiving report.
  - Unit prices on the invoice agree with those indicated on the disbursement document.
  - Extensions and footings are correct.
  - Written approval by the agency head or authorized designee authorizing payment appears on the disbursement document.

The *Memorandum of Understanding for Cooperative Disability Investigations (CDI)* states in part:

**Section IXB, fourth bullet: WSP Detectives and Office Assistant Senior (OAS)**

SSA will provide additional funding to the Washington DDS (as discussed above) to reimburse the WSP for the personnel costs incurred for their detectives and OAS assigned to the CDI Unit, including salary, fringe benefits, and overtime (if needed), and other allowable expenses identified in this agreement.

**Section IXC, first bullet: WSP Detective Vehicles**

The WSP will provide two official vehicles to the WSP detectives assigned to the CDI Unit. SSA agrees to provide the Washington DDS with funds to reimburse the WSP's costs and all routine operational expenses of those vehicles exclusively identified for program utilization, with the use of such vehicles restricted to CDI Unit official use only. WSP acknowledges that its detectives will be covered by the State's self-insurance program when operating the two assigned vehicles in the course and scope of their official duties.

**Section IXD, Other**

The SSA will fund CDI-specific training and travel and all other costs necessary to maintain and operate the Seattle CDI Unit effectively, subject to the liability conditions set forth in Sections VIII and IX of the MOU and subject to the availability of funds.

**State of Washington  
Corrective Action Plan**

***OMB Circular A-133 Audit  
For the Fiscal Year Ended  
June 30, 2005***

(This plan only addresses findings reportable under the revised OMB Circular A-133.)

**Department of Social and Health Services (DSHS)**

Fiscal Year	Finding Number	Finding and Corrective Action Plan					
05	41	<p>Finding:</p> <p>The Department of Social and Health Services, Division of Disability Determination Services, received reimbursement for unallowable costs for the Social Security Disability Insurance Program.</p> <p>Questioned Costs:</p> <table><thead><tr><th>CFDA #</th><th>Amount</th></tr></thead><tbody><tr><td>96.001</td><td>\$76,021</td></tr></tbody></table> <p>Status:</p> <p>Corrective action in progress.</p> <p>Corrective Action:</p> <p>The Memorandum of Understanding between the Washington State Patrol, Division of Disability Determination Services and Social Security Administration is valid until September 2006. The subsequent MOU will be revised to reflect allowable indirect costs that WSP can charge to SSA.</p> <p>The Division's administrative Fiscal Unit reviewed all WSP billings since inception of the program and determined that all costs were allowable (with the exception of indirect costs). However, the Division has asked the WSP to send payroll back-up documentation that matches their billings so that there is no confusion on what is being billed in the future.</p> <p>Completion Date:</p> <p>Estimated, October 2006</p>	CFDA #	Amount	96.001	\$76,021	
CFDA #	Amount						
96.001	\$76,021						

**05-29        The Department of Social and Health Services does not have adequate internal controls over the processing of expenditures through the Agency Financial Reporting System.**

**Background**

The Agency Financial Reporting System is the state of Washington's official accounting system. State agencies are required to enter their financial data, including accounts payable, into this System. The System has security features that, when used effectively, can reduce the risk of error or fraud in financial transactions.

Designated security administrators in each agency are responsible for determining the level of access granted to individuals within the agency and for removing access when appropriate. Access controls are available within the System to preclude any one person from having total control over a particular type of transaction.

We identified and reported internal control weaknesses related to access to the System in two previous Statewide Accountability Reports: Finding 03-15 in the fiscal year 2003 report and Finding 04-17 in the fiscal year 2004 report.

**Description of Condition**

This year we again reviewed to determine if the Department had improved access controls. We reviewed the types of System access the Department has granted to employees with accounts payable functions and found the Department still does not use the System's internal control features that allow for an adequate segregation of duties. Access to the accounts payable function is not secure, as described below.

- a. We found that 475 Department employees have incompatible duties, with the capability of entering and approving payment batches, bypassing management review. All of these employees could process a fictitious payment without oversight or approval by anyone.
- b. In addition, all 475 employees are capable of processing payments to unauthorized vendors by using certain designated codes intended for one-time, rather than recurring, payments. For fiscal year 2005, payments processed through these codes amounted to \$51,972,913. Such payments do not require that the vendor be formally and independently approved and established in the System. Instead, these 475 employees can set up any vendors they wish in the System and then generate payments to them with these codes. This condition creates a risk that employees could set themselves up as vendors for these one-time payments.
- c. We also noted numerous instances in which one-time payment codes were used for multiple payments to the same vendor. For instance, during the fiscal year the Department issued 46 warrants to one particular legitimate vendor using these codes. This condition increases the risk described in item b.
- d. The Department's System security administrators rely on management in the hundreds of Departmental offices to notify them of requests for access, changes in access, and terminations of access. Currently, this communication is not successful. We found access to the accounts payable function through the mainframe was still in place for four of the 10 former employees whose records we reviewed in detail.

**Cause of Condition**

The Department stated in its response last year that it did not concur with our concerns or recommendations. It believed it has adequate compensating controls for the weaknesses we found. We analyzed the Department's corrective action plan for the fiscal year 2004 finding and concluded that the controls it described as current did not adequately alleviate the risks.

However, the Department is establishing written policies and procedures that require an adequate separation of duties and timely access changes in any of its offices with an accounts payable function. We will review the adequacy of these policies and procedures during our next audit.

#### **Effect of Condition**

These control weaknesses increase to a high degree the risk that error or misappropriation could occur and not be detected by management in a timely manner, if at all.

#### **Recommendation**

We again recommend the Department develop and follow written policies and procedures for its accounts payable function that would ensure:

- An adequate separation of duties for those involved in making payments in the System.
- Timely changes to and removals from System access when appropriate.

#### **Department's Response**

*The Department partially concurs with this finding. As the Department responded the last two years, the finding is based solely on the review of system security accesses. There was not a review of compensating internal controls the Department has in place.*

*The finding asserts inadequate internal controls based solely on the Department's choice not to implement segregation of duties based on system access. The Department believes compensating controls are employed to provide sufficient internal control over the processing of expenditures. No audit evidence has been presented to assert the generally accepted compensating controls are insufficient.*

*The following are responses to each condition in the finding:*

- a. *Management has been addressing this issue since it became an audit finding. Over the past several months, DSHS has been reviewing AFRS access. Through the August 2005 - December 2005 timeframe, the following changes have occurred:*
  - *Staff with the ability to Input and Release a Batch has decreased 22%.*
  - *The total number of AFRS Users has decreased 17.5%.*

*In February 2006, a DSHS AFRS security policy, along with a new security form, was implemented. DSHS management at each location will apply the AFRS control of separation of input and release functions where applicable. Where this security level is not adopted, staff independent of the input and release function will perform a 100% review of all data processed. The control of 100% post review has been determined by DSHS management to be a stronger control in detecting irregular payments in that AFRS does not require the reviewer scroll through the items input prior to releasing a batch. Therefore, the batch releaser could just release the batch without performing any review and the only thing we accomplished was separating the input and release function.*

- b. *The Department partially concurs with the condition that via the use of certain designated codes (V0D1), employees can generate a warrant to anyone. The audit report does not identify testing of compensating controls to prevent this from occurring. Compensating controls are provided through separation of payment/warrant distribution from payment generation capabilities and the review of output reports and registers. In addition, headquarters' fiscal staff reviews the V0D1 usage quarterly, for improper usage. The agency will review the current processes/controls in place to determine if they can be strengthened even though the finding does not indicate that any payments were improperly made.*
- c. *The Department does not fully concur that there is an issue with making payments to a vendor through the V0D1 process. The agency is currently looking at ways to reduce the number of warrants generated by the V0D1 option, however, the complete elimination of this method of making payments will not occur because of*

*business needs. The use of making payments through VODI is appropriate for such items as making payments to other Washington governmental entities for garnishments, lost stolen warrant reissues, SSPS provider tax refunds and several other types of transactions that do not require registering the payee.*

- d. *The Department partially concurs with the condition that communication has not been successful to timely terminate system access for some terminated employees. Steps have been taken to identify those individuals with inappropriate access as well as improve the access documentation processes. In the Fiscal Year 2003 finding, SAO noted 40 cases. This year they noted 4 cases which illustrates the Department has been addressing this item. Efforts have been initiated to explore alternatives to relying solely on manager communication for access terminations. Such alternatives being reviewed include performing an agency AFRS user access review every April and October.*

#### Auditor's Concluding Remarks

We agree that the Department has some compensating controls in place which may detect errors or misappropriations after the fact. We are recommending a proper separation of duties in System access to help prevent errors or misappropriation from occurring. Since the Department issues billions of dollars in payments each year through the AFRS system, preventative controls are necessary. The Office of Financial Management has stated there is no System limit to the amount of one payment; therefore, an employee could input and release as large a check as desired for personal use and leave town before any of the Department's detection activities found the misappropriation. We reaffirm our finding and recommendations.

#### Applicable Laws and Regulations

The State of Washington Office of Financial Management's *State Administrative and Accounting Manual*, Section 20.20.20.a states in part:

Each agency director is responsible for establishing and maintaining an effective system of internal control throughout the agency.

Section 20.20.70.a states in part:

Control activities are the policies and procedures that help ensure management directives are carried out.

**Segregation of duties** - Duties are divided, or segregated, among different people to reduce the risk of error or inappropriate actions. For example, responsibilities for authorizing transactions, recording them, and handling the related assets should be separated.

# **Overview of the Office of the Inspector General**

The Office of the Inspector General (OIG) is comprised of our Office of Investigations (OI), Office of Audit (OA), Office of the Chief Counsel to the Inspector General (OCCIG), and Office of Resource Management (ORM). To ensure compliance with policies and procedures, internal controls, and professional standards, we also have a comprehensive Professional Responsibility and Quality Assurance program.

## **Office of Audit**

OA conducts and/or supervises financial and performance audits of the Social Security Administration's (SSA) programs and operations and makes recommendations to ensure program objectives are achieved effectively and efficiently. Financial audits assess whether SSA's financial statements fairly present SSA's financial position, results of operations, and cash flow. Performance audits review the economy, efficiency, and effectiveness of SSA's programs and operations. OA also conducts short-term management and program evaluations and projects on issues of concern to SSA, Congress, and the general public.

## **Office of Investigations**

OI conducts and coordinates investigative activity related to fraud, waste, abuse, and mismanagement in SSA programs and operations. This includes wrongdoing by applicants, beneficiaries, contractors, third parties, or SSA employees performing their official duties. This office serves as OIG liaison to the Department of Justice on all matters relating to the investigations of SSA programs and personnel. OI also conducts joint investigations with other Federal, State, and local law enforcement agencies.

## **Office of the Chief Counsel to the Inspector General**

OCCIG provides independent legal advice and counsel to the IG on various matters, including statutes, regulations, legislation, and policy directives. OCCIG also advises the IG on investigative procedures and techniques, as well as on legal implications and conclusions to be drawn from audit and investigative material. Finally, OCCIG administers the Civil Monetary Penalty program.

## **Office of Resource Management**

ORM supports OIG by providing information resource management and systems security. ORM also coordinates OIG's budget, procurement, telecommunications, facilities, and human resources. In addition, ORM is the focal point for OIG's strategic planning function and the development and implementation of performance measures required by the Government Performance and Results Act of 1993.