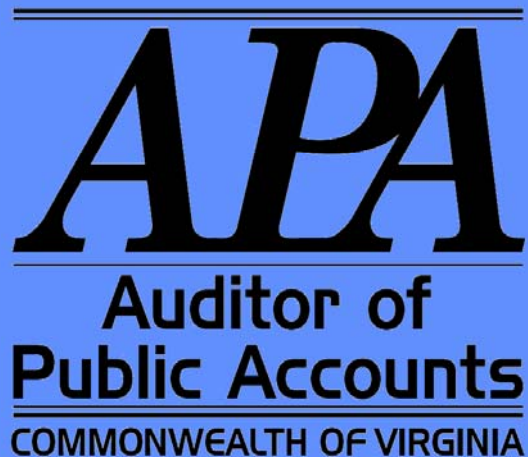


**DEPARTMENT OF VETERANS SERVICES
AND THE
VETERANS SERVICES FOUNDATION**

**REPORT ON AUDIT
FOR THE YEAR ENDED
JUNE 30, 2009**



AUDIT SUMMARY

Our audit of the Department of Veterans Services and the Veterans Services Foundation for the year ended June 30, 2009, found:

- proper recording and reporting of all transactions, in all material respects, in the Commonwealth Accounting and Reporting System;
- internal control matters that require management's attention and corrective action; these are located in the "Internal Control and Compliance Findings and Recommendation" section of this report beginning on page 2; and
- instances of noncompliance with applicable laws and regulations that are required to be reported; these are located in the "Internal Control and Compliance Findings and Recommendations" section of this report beginning on page 2.

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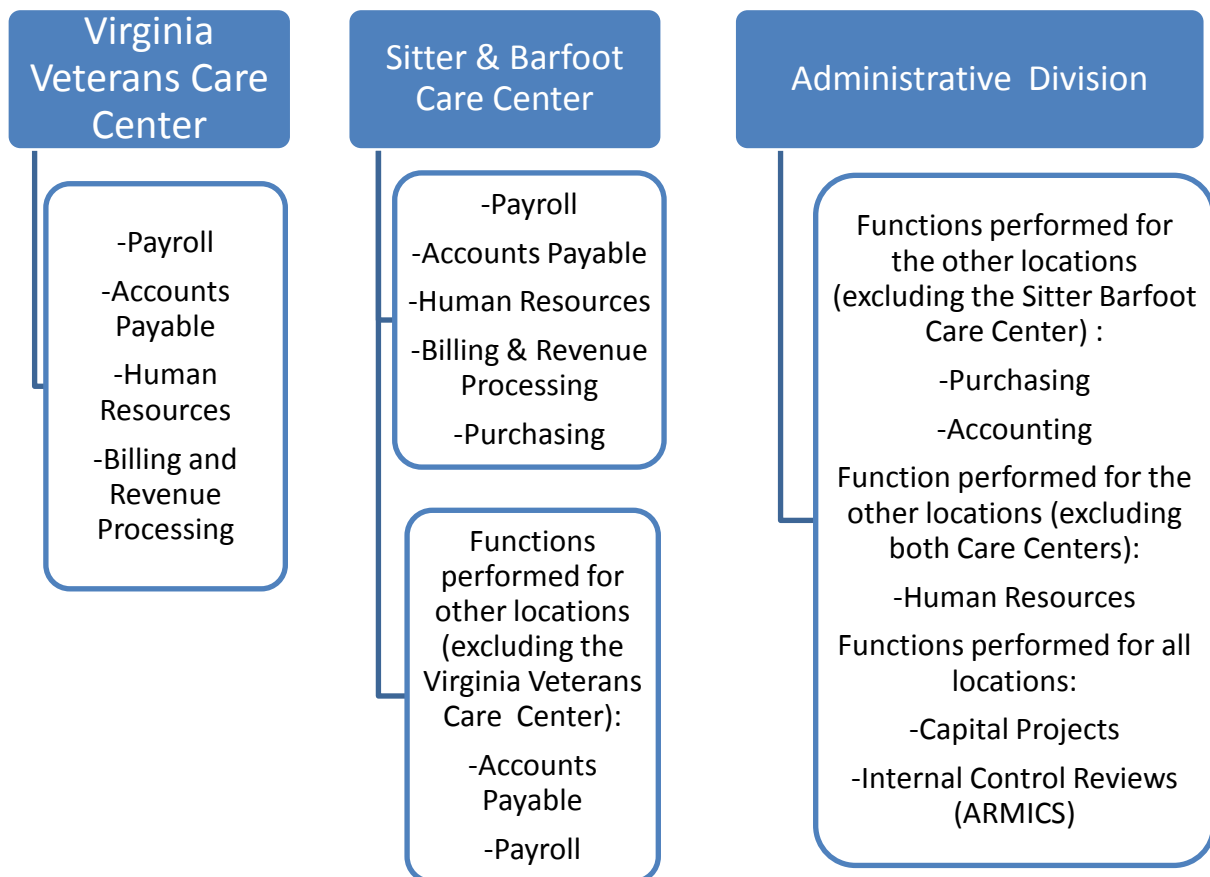
VETERANS SERVICES, A GROWING ORGANIZATION

The Virginia Department of Veterans Services (Veterans Services) consists of a central office, two cemeteries, two care centers, and 20 benefit offices located throughout the Commonwealth to provide veterans access to these services. Veterans Services is completing a third cemetery in 2010 and has submitted applications for federal funds to build and open two more care centers.

Administrative Services

Veterans Services is duplicating the administrative function throughout its organization. Veterans Services has an Administrative Division; additionally, the Virginia Veterans Care Center and the Sitter & Barfoot Care Center each have their own administrative staff. Furthermore, both the Administrative Division and the Sitter & Barfoot Care Center provide administrative services to the Veterans Services' other locations. The Administrative Division provides purchasing, accounting services, human resources, capital projects, and internal control reviews. The Sitter & Barfoot Care Center provides accounts payable and payroll services.

The following chart shows the current organization of Veterans Services administrative functions.



As the table above shows, Veterans Services duplicates several administrative functions including payroll, purchasing, and accounts payable. There is significant potential for streamlining and consolidating Veterans Services administrative functions in one location.

Currently, the two care centers account for 75 percent of Veterans Services' expenses. Before Veterans Services opens two more care centers, management should determine the most effective way to reorganize its administrative functions. An effective reorganization of Veterans Services' administrative functions will ensure the Department can devote appropriate resources on Virginia's veterans. Reorganizing its administrative functions will allow Veterans Services to improve its internal control structure while reducing its administrative expenses.

We previously recommended that management evaluate its operating environment and consider consolidating administrative functions in one location. As Veterans Services expands its physical footprint by opening new care centers and completing new cemeteries, its current decentralized environment may prevent the agency from achieving economies of scale.

INTERNAL CONTROL AND COMPLIANCE FINDINGS AND RECOMMENDATIONS

Evaluate the Agency Structure

Management should evaluate Veterans Services current organizational structure and consider consolidating as many administrative functions as possible. The U.S. Department of Veterans Affairs received additional funding as the result of the Federal Stimulus Act. This greatly increases the likelihood of available funding for new care centers in the immediate future.

As stated above, we have recommended that Veterans Services consolidate its administrative functions in the recent past. With a new cemetery due for completion by the end of 2010 and the increased likelihood of new care centers, Veterans Services' management should strongly consider the reorganization of its administrative functions. Management should determine the best structure for its administrative functions so that these functions do not limit Veterans Services' ability to expand services to veterans.

The use of a centralized office with sufficient staff and resources provides needed internal controls and management oversight of public resources. Management should consider a structure that can easily absorb both planned and unplanned expansions and fully consider opportunities for using technology to perform administrative functions rather than duplicating operations.

Improve the Information System Security Program

Although Veterans Services has made progress during the prior year, it does not yet have a complete Information Systems Security Program in place to protect its sensitive systems and data. Veterans Services has improved in the following areas.

- Created a Business Impact Analysis; however, it has not classified its data or identified whether the data is subject to regulatory standards, such as HIPAA, as required by Commonwealth IT standards.

- Developed a Risk Assessment, although it does not include one of the Department's major systems.
- Drafted its IT policies.

Although the security program is evolving, it is ineffective until management approves and implements the security policies. An information security program must use the information contained in a Business Impact Analysis and Risk Assessment. By not having sufficiently documented the data and whether it is subject to external regulatory oversight, and a risk management plan that includes all major systems, Veterans Services cannot develop a security plan that adequately addresses risks and safeguards data.

According to the Commonwealth's Security Policy, Veterans Services' Information Security Officer (ISO) is responsible for developing and managing the agency's IT Security Program and ensuring that the agency complies with its components. While there must be a collaborative effort between management, data owners, and the ISO to develop an agency's IT risk management plans, the ISO must ensure that the security program always meets current Commonwealth IT standards.

Until management approves Veteran Services' draft policies, there are no requirements for the ISO to enforce. We recommend that Veteran Services finalize its IT security policies and further develop its Business Impact Analysis and Risk Assessment. It should also update its contingency plans where needed to develop a security program that complies with the Commonwealth's security standards.

Improve and Implement HIPAA policies

While Veterans Services has developed some HIPAA policies and procedures, it needs to make improvements in several areas in order to comply with federal HIPAA regulations.

- Complete its Risk Assessment.
- Perform adequate system activity reviews.
- Undergo vulnerability testing.
- Test recovery from backup media.
- Ensure that system recovery time objectives accurately reflect business needs.

The Department processes the majority of the HIPAA-related data at Veterans Services' two care centers. The Information Security Officer (ISO) has the responsibility to develop and manage the agency's overall IT Security Program, including the HIPAA components, and ensure that the agency complies in all areas. There must be a collaborative effort between management, data owners, and the ISO to develop its HIPAA policies and procedures, the ISO must ensure that they always meet federal HIPAA regulations. Failure to comply with HIPAA can result in civil and criminal penalties. We recommend that Veterans Services further develop its HIPAA policies and procedures and incorporate the policies into its security awareness training program and follow-up to ensure compliance.

AGENCY HIGHLIGHTS

Veterans Services consists of an administrative division and five service delivery branches; benefits, cemeteries, care centers, veterans' education, and the Virginia Wounded Warrior Program. These branches work with three board-type entities – the Boards of Veterans Services, the Joint Leadership Council of Veterans Service Organizations, and the Veterans Services Foundation – to support the delivery of services to Virginia's veterans.

Benefits

The United States Department of Veterans Affairs provides benefits and services to veterans of the armed forces. These benefits include compensation for service-connected disability or death, income-based pensions, medical care, educational benefits, and home purchase assistance.

The Benefits Service Division assists Virginia's veterans in gaining information and access to the federal benefits and services for which they are eligible. The Benefits Service Division operates 20 field offices across Virginia to assist eligible veterans. In addition to the field offices, the division also operates numerous itinerant service points to serve veterans. Various government agencies and private entities provide the space for these additional service points.

Cemeteries

The Cemeteries Services Division operates two state-owned and operated cemeteries, the Virginia Veterans Cemetery in Amelia and the Albert G. Horton, Jr. Memorial Veterans Cemetery in Suffolk. These cemeteries provide burial and perpetual care services for veterans and their eligible dependents. Veterans Services is constructing a third cemetery in Southwest Virginia. The cemetery has four phases, and will add grave sites as needed with phase one scheduled for completion by fall 2010.

Veterans Education

Veterans Services is the U.S. Department of Veterans Affairs' State Approving Agency for Veterans Education (SAA). As the SAA, Veterans Services reviews, evaluates, and approves post-secondary education and training programs offered by educational institutions and various other entities within Virginia. Once a program receives approval, eligible veterans, war orphans, and widows may enroll in and receive financial assistance from the U.S. Department of Veterans Affairs while pursuing an approved course or program. Veterans Services monitors the approved education and training programs to ensure compliance with applicable federal and state regulations.

Veterans Services Foundation

The Veterans Services Foundation (Foundation) serves as an advisory foundation within the executive branch of state government. The Foundation raises funds, identifies existing revenue sources for veterans programs, and administers the Veterans Services Fund. Veterans Services' administrative division processes the Foundation's transactions. The Foundation spends funds on holiday gifts for the Care Center residents, activities, and other items for the veterans.

Care Centers

Veterans Services operates two care centers: the Virginia Veterans Care Center in Roanoke and the Sitter & Barfoot Veterans Care Center in Richmond. Veterans Services is anticipating receiving funding from the U. S. Department of Veterans Affairs to build a third care center in Hampton and has plans for a fourth care center in Northern Virginia. Veteran's Services will have to match 35 percent of the federal funds for the construction of the facilities as well as have approximately five million dollars in start up funds for each facility before the facilities would be self sufficient.

The Virginia Veterans Care Center provides long-term health care for up to 240 veterans in 120 semi-private rooms. Of the facility's 240 beds, 180 are skilled nursing care beds (including 60 set aside for Alzheimer's patients) and the remaining 60 beds are for assisted-living patients. Sitter-Barfoot Veterans Care Center provides long-term care for up to 160 veterans. All of the facility's 160 beds are single occupancy, skilled nursing care beds. Of the 160 beds, 40 beds are in a secure unit for Alzheimer's patients with an enclosed courtyard.

The Virginia Veterans Care Center receives no operating monies from the General Fund, operating entirely on revenues produced through caring for veterans. Revenue sources for both facilities include Medicaid, Medicare, per diem payments from the U.S. Department of Veterans Affairs, and private funding sources. The Sitter & Barfoot facility received a general fund appropriation in fiscal 2009, because the facility did not reach full capacity as quickly as expected and therefore revenues were not sufficient to cover all expenses. Management expects the facility's monthly revenue to cover its operating costs in future fiscal years.

The following table summarizes each care center's revenues, expenses, and populations for fiscal year 2009. The revenues and expenses per resident are higher for Sitter & Barfoot, because this facility has all skilled nursing beds whereas Virginia Veterans has 60 assisted living beds, which are much less expensive to staff than nursing beds. In addition Sitter & Barfoot had a full staff for all of fiscal year 2009, but was not at full patient capacity until March of 2009.

COMPARISON OF FACILITY OPERATIONS
Fiscal Year 2009
Long-term Care Facilities

	Sitter & Barfoot Veterans Care Center	Virginia Veterans Care Center
Average resident census	<u>115</u>	<u>213</u>
Total resident days	<u>44,910</u>	<u>77,690</u>
Revenue:		
Collections (institutional revenue)	\$ 9,586,057	\$12,378,900
Federal revenue	2,966,256	4,903,498
General fund appropriations	1,074,000	-
Other revenues	<u>-</u>	<u>4,752</u>
Total revenue	<u>13,626,313</u>	<u>17,287,150</u>
Expenses:		
Personal services	10,710,990	10,997,820
Contractual services	853,600	2,499,211
Supplies and materials	1,498,030	2,610,473
Continuous charges	275,108	1,006,366
Equipment	87,360	81,479
Plant and improvements	2,315	50,006
Transfer payments	<u>140,280</u>	<u>17,345</u>
Total expenses	<u>13,567,683</u>	<u>17,262,700</u>
Excess (deficiency) of revenues over expenses	<u>\$ 58,630</u>	<u>\$ 24,450</u>
Expenses per resident	<u>\$ 117,980</u>	<u>\$ 81,046</u>
Expenses per resident per day	<u>\$ 302</u>	<u>\$ 222</u>
Revenues per resident	<u>\$ 118,490</u>	<u>\$ 81,160</u>
Revenues per resident per day	<u>\$ 303</u>	<u>\$ 223</u>

Source(s): Commonwealth Accounting and Reporting System, 2009 Commissioner's Report

Financial Information

The following table summarizes Veterans Services' original and final budget and their actual expenses. Of the \$7.2 million variance between the final budget and actual expenses, about \$6.8 million (94 percent) is the difference between the final budget and actual expenses for the Care Center Operations. This resulted primarily because Sitter-Barfoot did not reach full occupancy until the last quarter of fiscal 2009. The care centers accounts for over 75 percent of Veterans Services' operating expenses.

Analysis of Budgeted to Actual Operating Expenses by Program for Fiscal Year 2009

<u>Program</u>	<u>Original Budget</u>	<u>Final Budget</u>	<u>Expenses</u>
Care center operations	\$28,535,091	\$37,645,130	\$30,830,383
Veterans benefits services	6,232,901	5,900,462	5,678,462
Administration and support	2,256,984	1,858,442	1,759,115
Cemetery management	1,106,447	1,229,892	1,163,435
Veterans education	<u>704,223</u>	<u>704,223</u>	<u>648,186</u>
Total	<u>\$38,835,646</u>	<u>\$47,338,149</u>	<u>\$40,079,581</u>

Source(s): Chapter 781 and the Commonwealth Accounting and Reporting System

The following table summarizes Veterans Services' fiscal 2009 operating expenses by type. Overall, personal services accounted for 68 percent of Veterans Services operating expenses in fiscal 2009.

Fiscal 2009 Operating Expenses by Type

Personal services	\$27,293,989	68%
Contractual services	4,402,479	11%
Supplies and materials	4,221,377	10%
Transfer payments	1,948,399	5%
Continuous charges	1,870,359	5%
All other types	<u>342,978</u>	<u>1%</u>
Total	<u>\$40,079,581</u>	<u>100%</u>

Source: Commonwealth Accounting and Reporting System

In addition to its operating expenses, Veterans Services had about \$1.1 million in capital project expenses. The following table provides detailed expenses for Veterans Services' four capital projects in fiscal 2009. Nearly 92 percent of total capital project expenses related to the development of a veterans cemetery in southwest Virginia.

Capital Project Expenses for Fiscal 2009

Southwest Virginia Veterans Cemetery	\$ 968,364
Acquisition of land for Hampton Roads Cemetery	75,290
Maintenance reserve	5,812
Sitter & Barfoot Veterans Care Center	<u>5,645</u>
Total capital project expenses	<u>\$1,055,111</u>

Source: Commonwealth Accounting and Reporting System



Commonwealth of Virginia

Walter J. Kucharski, Auditor

**Auditor of Public Accounts
P.O. Box 1295
Richmond, Virginia 23218**

April 8, 2010

The Honorable Robert F. McDonnell
Governor of Virginia

The Honorable M. Kirkland Cox
Chairman, Joint Legislative Audit
and Review Commission

We have audited the financial records and operations of the **Department of Veterans Services** for the year ended June 30, 2009. We conducted this performance audit 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.

Audit Objectives

Our audit's primary objectives were to evaluate the accuracy of recorded financial transactions on the Commonwealth Accounting and Reporting System, review the adequacy of the Department of Veterans Services internal controls, test compliance with applicable laws and regulations, and review corrective actions of audit findings from prior year reports.

Audit Scope and Methodology

Veterans Services' management has responsibility for establishing and maintaining internal control and complying with applicable laws and regulations. Internal control is a process designed to provide reasonable, but not absolute, assurance regarding the reliability of financial reporting, effectiveness and efficiency of operations, and compliance with applicable laws and regulations.

We gained an understanding of the overall internal controls, both automated and manual, sufficient to plan the audit. We considered significance and risk in determining the nature and extent of our audit procedures. Our review encompassed controls over the following significant cycles, classes of transactions, and account balances.

Expenses
Payroll
Appropriations

Collection of Receivables
Information Systems Security

We performed audit tests to determine whether Veterans Services' controls were adequate, had been placed in operation, and were being followed. Our audit also included tests of compliance with provisions of applicable laws and regulations. Our audit procedures included inquiries of appropriate personnel, inspection of documents, records, and contracts, and observation of Veterans Services' operations. We tested transactions and performed analytical procedures, including budgetary and trend analyses.

Conclusions

We found that the Veterans Services properly stated, in all material respects, the amounts recorded and reported in the Commonwealth Accounting and Reporting System. Veterans Services records its financial transactions on the cash basis of accounting, which is a comprehensive basis of accounting other than accounting principles generally accepted in the United States of America. The financial information presented in this report came directly from the Commonwealth Accounting and Reporting System.

We noted certain matters involving internal control and its operation and compliance with applicable laws and regulations that require management's attention and corrective action. These matters are described in the section entitled "Internal Control and Compliance Findings and Recommendations."

Veterans Services has taken adequate corrective action with respect to audit findings reported in the prior year that are not repeated in this letter.

Exit Conference and Report Distribution

We discussed this report with management on April 20, 2010. Management accepts the report and elected to not provide a response.

This report is intended for the information and use of the Governor and General Assembly, management, and the citizens of the Commonwealth of Virginia and is a public record.

AUDITOR OF PUBLIC ACCOUNTS

JDE/clj

DEPARTMENT OF VETERANS SERVICES

Vincent M. Burgess
Commissioner

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