**DEPARTMENT OF SOCIAL SERVICES**

**RICHMOND, VIRGINIA**

# REPORT ON AUDIT

# FOR THE YEAR ENDED

# JUNE 30, 1999

***AUDITOR OF***
***PUBLIC***
***ACCOUNTS***

***COMMONWEALTH OF VIRGINIA***

# AUDIT SUMMARY

Our audit of the Department of Social Services for the year ended June 30, 1999, found:

- amounts reported in the Commonwealth Accounting and Reporting System were fairly stated;

- one material weakness in internal control and its operation entitled "Properly Record Year-End Liabilities";

- certain other matters in internal control and its operation that we consider reportable conditions;

- no instances of noncompliance with the selected provisions of applicable laws and regulations; and

- corrective action of prior audit findings, except for the finding entitled "Properly Charge Payroll to Federal Programs".

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February 4, 2000

The Honorable James S. Gilmore, III
Governor of Virginia
State Capitol
Richmond, Virginia

The Honorable Richard J. Holland
Chairman, Joint Legislative Audit
and Review Commission
General Assembly Building
Richmond, Virginia

INDEPENDENT AUDITOR'S REPORT

We have audited the financial records and operations of the **Department of Social Services** for the year ended June 30, 1999. We conducted our audit in accordance with Government Auditing Standards, issued by the Comptroller General of the United States.

Audit Objective, Scope, and Methodology

Our audit's primary objectives were to evaluate the accuracy of recording financial transactions on the Commonwealth Accounting and Reporting System and in the Department's accounting records, review the adequacy of the Department's internal control, and test compliance with applicable laws and regulations. We also reviewed the Department's corrective actions on audit findings from prior year's reports.

Our audit procedures included inquiries of appropriate personnel, inspection of documents and records, and observation of the Department's operations. We also tested transactions and performed such other auditing procedures, as we considered necessary to achieve our objectives. We reviewed the overall internal accounting controls, including controls for administering compliance with applicable laws and regulations. Our review encompassed controls over the following significant cycles, class of transactions, and account balances:

Federal Grants
Expenditures
Accounts Payable
Revenue
Payroll

We obtained an understanding of the relevant internal control components sufficient to plan the audit. We considered materiality and control risk in determining the nature and extent of our audit procedures. We performed audit tests to determine whether the Department's 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.

The Department's 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.

Our audit was more limited than would be necessary to provide assurance on internal control or to provide an opinion on overall compliance with laws and regulations. Because of inherent limitations in internal control, errors, irregularities, or noncompliance may nevertheless occur and not be detected. Also, projecting the evaluation of internal control to future periods is subject to the risk that the controls may become inadequate because of changes in conditions or that the effectiveness of the design and operation of controls may deteriorate.

Audit Conclusions

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

We noted certain matters involving internal control and its operation that we considered to be reportable conditions. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of internal control that, in our judgment, could adversely affect the Department's ability to record, process, summarize, and report financial data consistent with the assertions of management in the financial records. Reportable conditions entitled "Properly Record Year-End Liabilities", "Properly Charge Payroll to Federal Programs", "Segregate Duties over Cost Allocation Process", "Strengthen Security over Critical Production Databases", "Strengthen Energy Assistance Program System Controls," and "Improve Usage of Income Eligibility Verification System" are discussed in the subsection "Internal Control and Compliance Findings and Recommendations." However, of the reportable conditions described above, we consider "Properly Record Year-End Liabilities" to be a material weakness.

A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relation to the financial information being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses.

The results of our tests of compliance with applicable laws and regulations disclosed no instances that we are required to be reported under Government Auditing Standards.

The Department has not taken adequate corrective action with respect to the previously reported finding, "Properly Charge Payroll to Federal Programs." Accordingly, we included this finding in the section entitled "Internal Controls and Compliance Findings and Recommendations." The Department has taken corrective action with respect to audit findings reported in the prior year that are not repeated in this report.

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

## EXIT CONFERENCE

We discussed this report with management at an exit conference held on March 2, 2000.

AUDITOR OF PUBLIC ACCOUNTS

LCR:whb
whb:53

## INTERNAL CONTROL AND COMPLIANCE FINDINGS AND RECOMMENDATIONS

### Properly Record Year End Liabilities

The Acting Controller erroneously changed the recording of a $35 million liability for the June 1999, locality reimbursement. As a result, the Department's year-end liabilities reported to the State Controller were understated by $35 million. While the net effect of this error did not significantly affect the Commonwealth's annual financial report, it does, however, raise questions about the Department's ability to prepare accurate financial information. The Commonwealth's annual financial report serves as the basis of public accountability and is a tool of rating agencies to set the state's interest rate on bonds. It is therefore essential that all individuals and agencies provide the State Controller with accurate and timely information.

Finally, the Department has had three different individuals acting in the Controller position since May 1998. We understand the Department is in the process of permanently filling the position. Management should ensure the individual given the position has both experience and the management skills to improve the Department's ability to provide accurate and timely information. We suggest that management use the State Controller's staff in evaluating candidates for this position.

### Properly Charge Payroll to Federal Programs

As reported in our last two reports, Division of Information Systems (DIS) employees did not record all hours worked in the DIS time tracking system. We found 16 of 36 employees tested did not record all time worked in the system. Consequently, the system understated total hours worked, and staff had to recompute statistics and prepare adjustments. DIS uses the time tracking system to allocate the division's payroll expenses to Federal programs. Incomplete or inaccurate information in this system can result in incorrect allocations of costs.

45 CFR Part 74.22, "Allowable Costs," requires states to determine allowable costs in accordance with OMB Circular A-87, "Cost Principles for State and Local Governments." These principles require appropriate time and distribution records to support salaries and wages of employees chargeable to more than one grant program or other cost objective.

DIS procedures require that all employees enter their time worked into the system, and DIS managers must certify that all hours worked are in the system. The Department should ensure that managers are following these internal policies and procedures. The Division of Finance should prepare the quarterly cost allocation only after they ensured DIS employees have recorded all of their time.

### Segregate Duties over Cost Allocation Process

The Department has not segregated critical duties in the cost allocation process and one employee performs most of the accounting functions. The Department uses a cost allocation process to distribute almost $400 million in indirect expenses to federal programs each year. In fiscal 1999, one employee recorded cost allocation adjustments, reconciled and reviewed balances, and had the capability to change the cost allocation module. The Department has not adequately segregated these critical duties, thus putting themselves at risk that errors and misstatements could occur and go undetected.

In fiscal 1999, the Department had significant employee turnover in the Division of Finance, which may have contributed to their inability to properly segregate these duties. We recommend the Department fill critical financial management positions in order to ensure appropriate supervisory review over the cost allocation process. Additionally, the Division should cross-train personnel to ensure all individuals have working knowledge of this critical area and not depend upon one individual.

Strengthen Security over Critical Production Databases

We identified security weaknesses in the financial and On-line Automated Services Information System (OASIS) databases. The financial database contains critical financial information while the OASIS database contains foster care, adoption, and child protective services case information. Below are these security weaknesses and our recommendations.

- The financial and OASIS databases contain settings that allow certain users to connect to the database without the use of a password. The REMOTE_OS_AUTHEN parameter for both databases has a TRUE setting. This allows users with external authentication to connect to the databases using the SQL*Plus tool without a password. Each of the user IDs defined as having external authentication has privileges that would allow an unauthorized user to compromise the integrity of the databases. The Department should change the setting of the REMOTE_OS_AUTHEN parameter to FALSE.

- The Database Administrators share an account to perform database functions. The Department should assign each individual their own user account within the databases. Furthermore, the Department should consider using the Oracle audit function to monitor activity of Database Administrators. The Oracle audit function allows the Security Officer to determine when anyone has performed unauthorized actions and provides an additional control for monitoring changes to the database. Enabling full audit capability adds to the processing required by the system and may have an adverse effect on system performance. Due to system performance concerns, we recommend that the Department begin by auditing the alter and drop actions. When system performance allows for expansion of the auditing capability, the Department should consider expanding the feature. Assigning each individual that performs database functions their own ID and using the audit function to monitor their activities will provide for increased accountability on these critical databases.

Strengthen Energy Assistance Program System Controls

The production data files for the Energy Assistance Program (EAP) system are located in the test environment instead of the production environment. Programmers or other users with a certain mode capability in the test environment can make changes to the production data files. This increases the likelihood of individuals making unauthorized changes and compromising the integrity of critical data. The Department has recognized the risks associated with this deficiency and plans to redesign the EAP system in May 2000. The Department should continue their efforts towards redesigning this system and strengthening the system controls.

Improve Usage of Income Eligibility Verification System

The Department does not use the information obtained from the Income Eligibility and Verification System (IEVS) to verify income for TANF recipients. OMB Circular A-133 and section 1137 of the Social Security Act require the State to participate in the IEVS. The Department is required to coordinate data exchanges with other federally assisted benefit programs, and use income and benefit information when making eligibility determinations for TANF recipients. DSS performs quality control reviews to ensure the security of the IEVS reports, but does not monitor whether the local social service agencies actually use the information. The Department should implement procedures for properly examining the information provided from the IEVS. In addition, the Department should review whether the local social service agencies are performing the necessary information checks on TANF recipients.

## AGENCY BACKGROUND

The Department provides benefits and services to help low-income families move from dependence to self-sufficiency. The Department provides these benefits and services through many programs including Temporary Assistance for Needy Families (TANF), Food Stamps, Protective Services programs for adults and children, and Medicaid eligibility determinations. The Department also establishes child support obligations, and collects and disburses the child support payments. In administering these programs, the Department provides funds to 123 local social service agencies for service delivery and eligibility determination for many of these programs. The following table shows statewide caseload data for several Social Services programs over the last five years. There have been significant changes in the TANF and Child Day Care caseloads. The reductions in the TANF caseload and the increase in the child day care caseload represent changes since the agency enacted welfare reform efforts in 1995.

| | **TANF** | **Foster Care** | **Child Day Care** | **Food Stamps** | **Child Support Enforcement** |
|---|---|---|---|---|---|
| 1995 | 73,033 | 6,841 | 18,312 | 233,389 | 364,598 |
| 1996 | 66,177 | 7,201 | 22,651 | 234,853 | 387,459 |
| 1997 | 56,256 | 7,446 | 21,981 | 215,871 | 405,490 |
| 1998 | 44,091 | 7,756 | 25,505 | 176,044 | 415,149 |
| 1999 | 37,798 | 8,292 | 35,668 | 160,147 | 417,098 |

Source: VDSS Information Resource Book (TANF, Child Day Care and Food Stamps caseloads are based on monthly averages)

The Department has a central office in Richmond, five regional offices, and 18 child support enforcement district offices across the state. Within the department, there are over 1,500 employees statewide. The Department experienced many organizational and personnel changes in fiscal 1999 in the Division of Finance. Due to the reassignment and subsequent resignation of the Controller, there have been three different individuals acting as Controller since May 1998. In addition, several positions in the division have been vacant or had personnel changes during the year. Overall, this division was not fully staffed and lacked consistent personnel in key positions over the last year.

The Department has also had organizational and personnel changes in senior management positions which have continued into fiscal 2000. During the year, the Department hired a Chief Deputy Director. With the agency director's resignation in January 2000, the Chief Deputy Director is now the acting Director and a Director of Planning was appointed.

## FINANCIAL INFORMATION

The Department's funding is a combination of state, federal and special funds. Most of the agency's revenues come from three sources – general fund appropriations, child support collections, and federal grants. In fiscal 1999, the Department received over $1 billion in revenue, including General Fund appropriations of $238 million, child support payments of $338 million and federal grants of $450 million. The federal grant revenue comes from many different federal programs, all with their own federal requirements.

In fiscal 1999, the Department had total expenses of over $1 billion. The majority of the department's expenses are TANF-related benefit payments, child support payments, and transfers to local social services agencies. The following table shows fiscal 1999 expenses by program, including the original and adjusted budgets.

| Program | Original Budget | Adjusted Budget | Actual Expenses |
|---|---|---|---|
| Temporary Income Supplement Services | $ 146,325,076 | $ 156,799,755 | $ 146,455,814 |
| Protective Services | 51,090,800 | 52,577,730 | 52,454,679 |
| Financial Assistance to Local Welfare/Social Services Boards for Administration of Benefit Programs | 129,624,487 | 127,224,487 | 121,512,416 |
| Continuing Income Assistance Services | 17,253,329 | 17,533,329 | 17,526,352 |
| Employment Assistance Services | 63,194,804 | 76,483,343 | 69,347,550 |
| Child Support Enforcement | 353,041,613 | 407,141,613 | 386,032,507 |
| Medical Assistance Services (Non-Medicaid) | - | 793,014 | 793,014 |
| Administrative and Support Services | 43,902,590 | 53,376,018 | 52,506,453 |
| Financial Assistance for Individual and Family Services | 191,698,427 | 196,698,427 | 189,949,539 |
| Regulation of Public Facilities and Services | 6,419,259 | 6,419,259 | 5,885,149 |
| Total expenses | $ 1,002,550,385 | $ 1,095,046,975 | $ 1,042,463,473 |

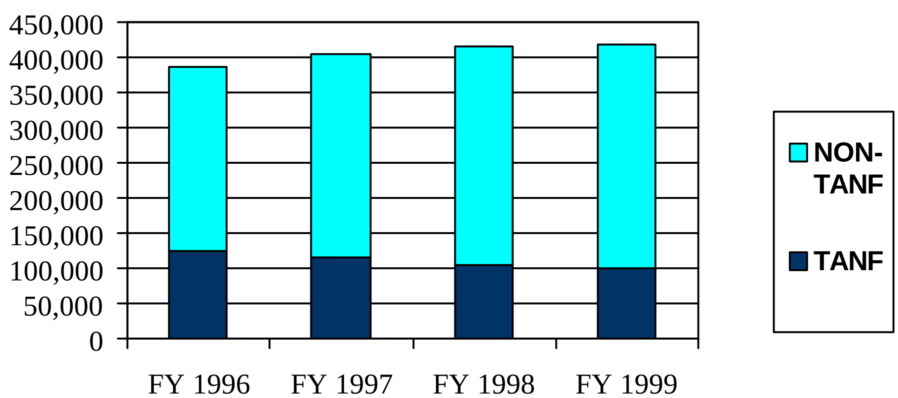
(Source: CARS data and Chapter 924 of Virginia Acts of Assembly)

The table above shows significant adjustments to original budgets in several programs. The effects of welfare reform have been difficult to predict causing needed adjustments to the Department's original budgets. The Department increased the original budget for the Employment Assistance Services program by $13 million to reflect a carryforward balance and an appropriation transfer from another program.

The Department also adjusted the original budget for the Child Support Enforcement (CSE) program by more than $50 million. This adjustment reflected additional appropriations and a transfer from another program to cover an estimated $2.5 million shortfall. In the past, the program has realized a profit, which it transferred to the General Fund at the end of the year; however, there have been significant changes in the CSE program over the last several years due to state and federal welfare reform efforts. Some of these changes have affected the program's ability to generate a profit. For example, under federal welfare reform, the federal government stopped mandating and funding disregard payments. The Department has continued to make the disregard payments, which has increased CSE expenses, thus resulting in decreased profit. Disregard payments totaled $3.8 million in fiscal 1999.

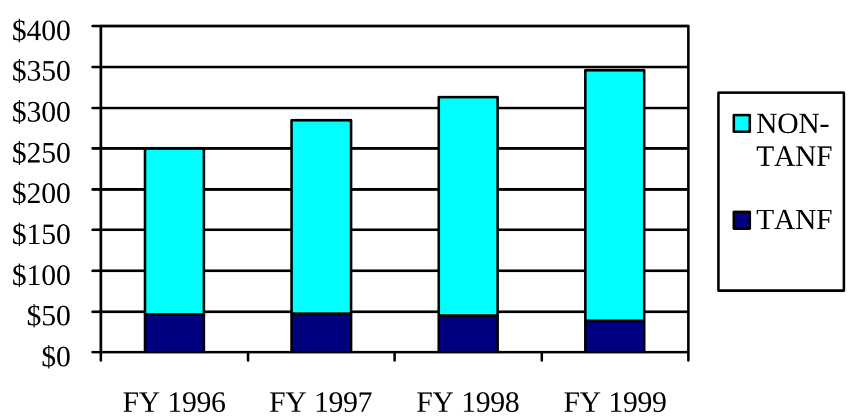
In addition, welfare reform efforts have significantly affected the CSE caseloads. Although the total caseload has increased over the last four years, the number of TANF cases has decreased with welfare reform, which in turn, has affected the amount of retained collections and incentive payments the Department can receive from the federal government. The federal government pays incentives to States based on the amount of TANF collections. With decreasing TANF caseloads and collections, the amount of incentives the Department has received has decreased. The division received $5.1 million in incentives during fiscal year 1999. The graphs below illustrate the changes in the CSE caseload and collections over the last four years. The Department expects the TANF caseload to continue to decline.

CHILD SUPPORT ENFORCEMENT CASELOAD




CHILD SUPPORT ENFORCEMENT COLLECTIONS

(rounded to the millions)



The Department also oversees the issuance of food stamps across the state which totaled over $287 million in fiscal 1999. The Department faces potential federal sanctions of $15.6 million for exceeding acceptable food stamp error rates set by the federal government. Amendments to the Food Stamp Act of 1977 allow states subject to potential error rate sanctions to either make a direct repayment to the federal government or to reinvest the funds in program administration improvements. The Department has developed a reinvestment plan for the program, and has a settlement agreement with the federal government; however, it is possible that the Department may incur additional liabilities for federal fiscal year 1999 error rates. The Department is reviewing the food stamp eligibility determination process in an effort to find ways to reduce errors.

## STATUS OF INFORMATION SYSTEMS INITIATIVES

The Department is currently working on several information systems initiatives. Each of these is discussed in more detail below.

### Application Benefit Delivery Automation Project

The Application Benefit Delivery Automation Project (ADAPT) system performs eligibility determinations and benefit calculations at local social services agencies for TANF, Food Stamps, and Medicaid. Local social services agencies have converted all TANF and Food Stamp cases to ADAPT. The Department will pilot the Medicaid module of ADAPT in the Newport News social services agency in March 2000.

In fiscal 1999, the ADAPT system experienced slow processing times and complete shutdowns. These problems were a result of the increased conversion of cases and network traffic. The Department is currently working with the Department of Information Technology (DIT) to resolve these issues. DIT is currently negotiating a statewide telecommunications contract that would increase capacity for DSS, as well as other agencies. DIT expects to award the contract in March 2000. The Department has also taken other steps to improve ADAPT including working with localities to upgrade their connections, offering advanced training sessions and operating an ADAPT help desk.

The Department expects to complete the ADAPT project in fiscal 2002 at a total cost of $77 million. This amount includes both recurring costs ($52 million) and developmental costs ($25 million) through fiscal year 2003. Through June 30, 1999, total costs are $43 million, including $21 million of developmental costs.

### Electronic Benefits Transfer

Federal welfare reform legislation requires the Commonwealth implement an Electronic Benefits Transfer (EBT) system to disburse food stamp benefits by October 1, 2002. As of June 1999, Virginia is one of only four states that has neither a system already in place nor a contract to purchase a system. The Department originally issued a Request for Proposal (RFP) in January 1997. They received bids on this proposal but subsequently canceled the RFP due to cost neutrality issues. The Department modified the RFP and re-issued it in August 1999. The Department is currently evaluating bids received and expects to award the contract in April 2000. The Department does not have a contingency plan for the delivery of food stamp benefits in the event that the system is not fully operational by October 2002.

Federal guidelines for implementing EBT are that they will maintain the level of funding for administration of food stamps consistent with expenses prior to EBT. Recent experience by other states indicates that because of caseload declines, this level of funding is not always sufficient. The Department is working closely with the federal government and other states to ensure proper planning for funding of EBT.

Financial Accounting Automated System

The Department implemented a new financial management system, FAAS, in July 1999. The Department is currently using the general ledger, accounts payable and purchasing modules of the new system. They are in the process of evaluating some of the other modules to determine whether the agency will fully implement these.

On-line Automated Services Information System

The Department's On-line Automated Services Information System (OASIS) is a case management system for foster care, adoption, and other child protective cases. As of July 1999, OASIS included all foster care, adoption, and child protective services cases. The Department is currently working on expanding the functionality of OASIS to include Child Day Care and Adult Services cases.

The federal government fined the Department $82,000 for foster care reporting problems with OASIS. The Department is partnering with several other states in appealing these fines. Additionally, Social Services has not been successful in having the federal government pay for their share of OASIS, estimated at $7.5 million. The Department has identified other funds to pay for this system.

Automation Program to Enforce Child Support

The Automation Program to Enforce Child Support (APECS) system tracks financial and case management information for child support cases. The Department is continuing to modify APECS for changes required for welfare reform. New hardware and software have significantly decreased month-end batch processing time and reduced user downtime.