STATE OF TENNESSEE
DEPARTMENT OF HUMAN SERVICES
TENNESSEE REHABILITATION SERVICES
1405-A BROOKWOOD AVENUE
FRANKLIN, TENNESSEE 37064

TELEPHONE: 615-595-2071 FAX: 615-790-5972

www.tn.gov/humanservices

BILL LEE
GOVERNOR

DANIELLE W. BARNES
COMMISSIONER

March 08, 2019

Ms. Kristine Tallent
Assistant City Administrator/CFO
109 Third Avenue South
Franklin, TN 37064

Received
MAR 15
Finance

Dear Ms. Tallent:

The Tennessee Rehabilitation Center at Franklin is requesting $23,170.00 for the 2019-2020 fiscal year which is the same amount approved for the 2018-2019 fiscal year.

Enclosed is the completed "Non-Profit Organization Request for City of Franklin," and a copy of the most recent state audit report.

We greatly appreciate the support and assistance the City of Franklin has provided in the past. We hope the City of Franklin will be able to continue their assistance by funding this request for fiscal year 2019-2020. If you should have any questions, or need further assistance, please call our center at (615)790-5509.

Sincerely,

Selina Kirkland
Tennessee Rehabilitation Center at Franklin, Manager
1405-A Brookwood Avenue
Franklin, TN 37064
615-595-2071

NON-PROFIT ORGANIZATION
REQUEST FOR CITY OF FRANKLIN FUNDS
2019-20 FISCAL YEAR

Organization Name: Tennessee Rehabilitation Center at Franklin Phone: 615-790-5509
Contact Person & Title: Selina Kirkland, Manager
Mailing Address: 1405-A Brookwood Avenue, Franklin, TN 37064
Federal Identification # (if applicable): N/A
E-mail address: Selina.Kirkland@tn.gov

Number of Active Participants in Organization: 120

If necessary, use separate sheet to provide requested information.

Does this organization charge fees to participants? Yes _____ No X
If yes, please itemize the structure utilized:

If no, please explain: Funding received from the City of Franklin and Williamson County is matched with federal monies to provide services to individuals with significant disabilities living in Williamson County. No fees are charged to the client.

Please provide the approximate number of clients served by your program on a yearly basis: 130. All funds provided by the Williamson County Commission must be used to provide assistance to Williamson County citizens only. Please provide documentation to show the expenses used for service to Williamson County citizens:

All clients served by the Tennessee Rehabilitation Center at Franklin are Williamson County residents. During FY 18-19, 130 individuals with disabilities were served.

List ANY agency (or agencies) in Williamson County which you consider may directly, or indirectly, provide the same or similar services as those provided by your agency. If such an agency exists, please list the similarities:

Waves, Inc. is a residential day program providing employment services to individuals with severe cognitive disabilities. They are a fee for service agency and require participants to be recipients of Social Security Disability benefits.
Center for Living and Learning is a residential facility providing employment services to individuals with severe and emotional disabilities. The center is a fee-for-service agency.

Unless prohibited by law, please provide documentation that your organization made a good faith effort to collect donations from private sources. The Tennessee Rehabilitation Center at Franklin receives local funding that is matched with federal dollars and is administered by the State of Tennessee. The State of Tennessee does not permit fundraising.

Non-Profit Organization Request for City of Franklin Funds - Page Two
Organization: Tennessee Rehabilitation Center at Franklin

EXPENDITURES:	Avg FY18 & FY 17 Actuals	FY 19 budget	Proposed FY20 Budget
Travel	1,845	5,000	1,900
Printing and Duplicating		100	-
Utilities and Fuel	5,617	7,500	6,700
Communications	6	200	-
Maint. & Repairs	4,733	7,400	4,400
Prof Services Third Party	1,298	2,600	2,700
Supplies and Materials	1,090	3,000	900
Rentals and Insurance	87,513	90,000	88,400
Motor Vehicle Operation	-	200	-
Awards and Indemnities	-	-	-
Grants and Subsidies	686	3,000	1,000
Unclassified	-	-	-
Inventory	(235)	-	-
Equipment	-	-	-
Land	-	-	-
Buildings	-	-	-
Training	28	200	-
Data Processing	860	800	1,100
Prof Services by State Agency	14,364	10,000	12,500
Operational Total	117,807	130,000	119,600
GRAND TOTAL	192,140	351,700	302,600

Non-Profit Organization Request for City of Franklin Funds - Page Three
Organization: Tennessee Rehabilitation Center at Franklin

REVENUES:	Actual 2017-18	Expended 2018-2019	Requested 2019-2020
Williamson County Government	67,816	67,816	67,816
City of Franklin	23,170	23,170	23,170
Federal Government	278,972	278,972	279,972
TOTAL REVENUES	369,958	369,958	369,958

Personnel & Salary Information

PERSONNEL:	**Avg FY18 Actuals & FY17 Actual**	**FY19 Budget**	**Proposed FY20 Budget**
Salaries and Wages	52,849	171,700	123,100
Longevity	526	2000	1,600
Overtime			
Employee Benefits	20,958	48,000	58,300
Payroll Total	74,333	221,700	183,000

List any equipment owned by this organization funded, in whole or in part, by Williamson County. Please indicate what it is used for, how it is maintained and where it is stored (use a separate sheet if necessary): N/A

City of Franklin
APPLICATION ADDENDUM

For the funding year, July 1, 2019 through June 30, 2020

Name of Agency: Tennessee Rehabilitation Center at Franklin
Date: March 8, 2019

Please provide a detailed description of the proposed use of funds that the City of Franklin might provide for Fiscal Year 2018:

Funds allocated by the City of Franklin to the Tennessee Rehabilitation Center at Franklin will be used to cover the administrative operational cost associated with providing no cost services in the form of Vocational Evaluations, Employee Development Services, and Job Placement assistance to eligible individuals with significant disabilities who are interested in obtaining employment.

Please provide information on any interaction that your agency has with the operations of City Of Franklin departments (e.g., response to calls from Police after domestic incidents, provision of meals or lodging to displaced persons, etc.):

During the past fiscal year, the Tennessee Rehabilitation Center at Franklin had no interaction with the departments of the City of Franklin.

Please answer completely the following questions using additional pages if necessary:

1. **Specifically what services did your agency provide <u>last year</u> for which you are requesting funding this year? What were the objectives and results? (Include description capacity, intensity and duration of services.)**

   The Tennessee Rehabilitation Center at Franklin provided the following services last year:

   1. <u>Comprehensive Vocational Evaluation Services</u>
   a) Assists in discovery of vocational interests, strengths, and weaknesses as well as the type of jobs or training in which the client can best perform.
   b) Determines employment aptitudes, interests and abilities.
   c) Involves career exploration and planning.
   d) Observation of work habits and behaviors.

   2. <u>Employee Development Services</u>
   a) Assists with building physical work tolerance.
   b) Teaches valuable employment skills and allows client to gain actual work experience.
   d) Education through classes on various life skill topics such as budgeting, interviewing, independent living skills and application of basic computer skills.

   3. <u>Job Readiness, Job Development, and Community Employment Placement Assistance</u>
   a) Job Readiness instruction, resume creation, job development, interview skills practice, online job searching/applications, and assistance with completing applications.
   b) Job Coaching services.
   c) Job Retention services.
   d) Supported Employment Services.

2. **Are there procedures in place for measuring the results achieved by your agency? If so, provide detailed data.**

   The state of Tennessee requires the Tennessee Rehabilitation Center at Franklin to provide monthly statistical information documenting program utilizations and successful outcomes.

3. **Does your agency receive any external quality review or accreditation? If so, provide a copy of certificate or license and please explain.**

   The Counsel on Accreditation of Rehabilitation Facilities (CARF) has accredited this agency through 2019.

4. **What percent of your local agency budget is your allocation request from the City of Franklin?**

   The allocation request of $23,170 from the City of Franklin represents 25% of the administrative budget of the Tennessee Rehabilitation Center at Franklin.

5. **What other fundraising activities does your agency engage in during the year?**

   The Tennessee Rehabilitation Center at Franklin does not participate in any fundraising.

6. **Do you charge any fees for your services?**

   The Tennessee Rehabilitation Center does not charge for services.

carf INTERNATIONAL

November 29, 2016

Pam Furlong
Middle Tennessee Rehabilitation Center Network
1132 Haley Road
Murfreesboro, TN 37129

Dear Ms. Furlong:

It is my pleasure to inform you that Middle Tennessee Rehabilitation Center Network has been issued CARF accreditation based on its recent survey. The Three-Year Accreditation applies to the following service(s):

Community Employment Services: Job Development
Comprehensive Vocational Evaluation Services
Employee Development Services

This accreditation will extend through October 31, 2019. This achievement is an indication of your organization's dedication and commitment to improving the quality of the lives of the persons served. Services, personnel, and documentation clearly indicate an established pattern of conformance to standards.

The survey report is intended to support a continuation of the quality improvement of your organization's service(s). It contains comments on your organization's strengths as well as any consultation and recommendations. A quality improvement plan (QIP) demonstrating your organization's efforts to implement the survey recommendation(s) must be submitted within the next 90 days to retain accreditation. The QIP form is posted on Customer Connect (*customerconnect.carf.org*), CARF's secure, dedicated website for accredited organizations and organizations seeking accreditation. Please log on to Customer Connect and follow the guidelines contained in the QIP form.

Your organization should take pride in achieving this high level of accreditation. CARF will recognize this accomplishment in its listing of organizations with accreditation and encourages your organization to make its accreditation known throughout the community. Communication of the accreditation to your referral and funding sources, the media, and local and federal government officials can promote and distinguish your organization. Enclosed are some materials that will help you publicize this achievement.

Your organization's complimentary accreditation certificate will be sent separately. You may use the enclosed form to order additional certificates.

If you have any questions regarding your organization's accreditation or the QIP, you are encouraged to seek support from John Hannon by email at jhannon@carf.org or telephone at (888) 281-6531, extension 7198.

CARF International Headquarters
6951 E. Southpoint Road
Tucson, AZ 85756-9407, USA

www.carf.org

CARF encourages your organization to continue fully and productively using the CARF standards as part of its ongoing commitment to accreditation. CARF commends your organization's commitment and consistent efforts to improve the quality of its service(s) and looks forward to working with your organization in its ongoing pursuit of excellence.

Sincerely,

Brian J. Boon, Ph.D.

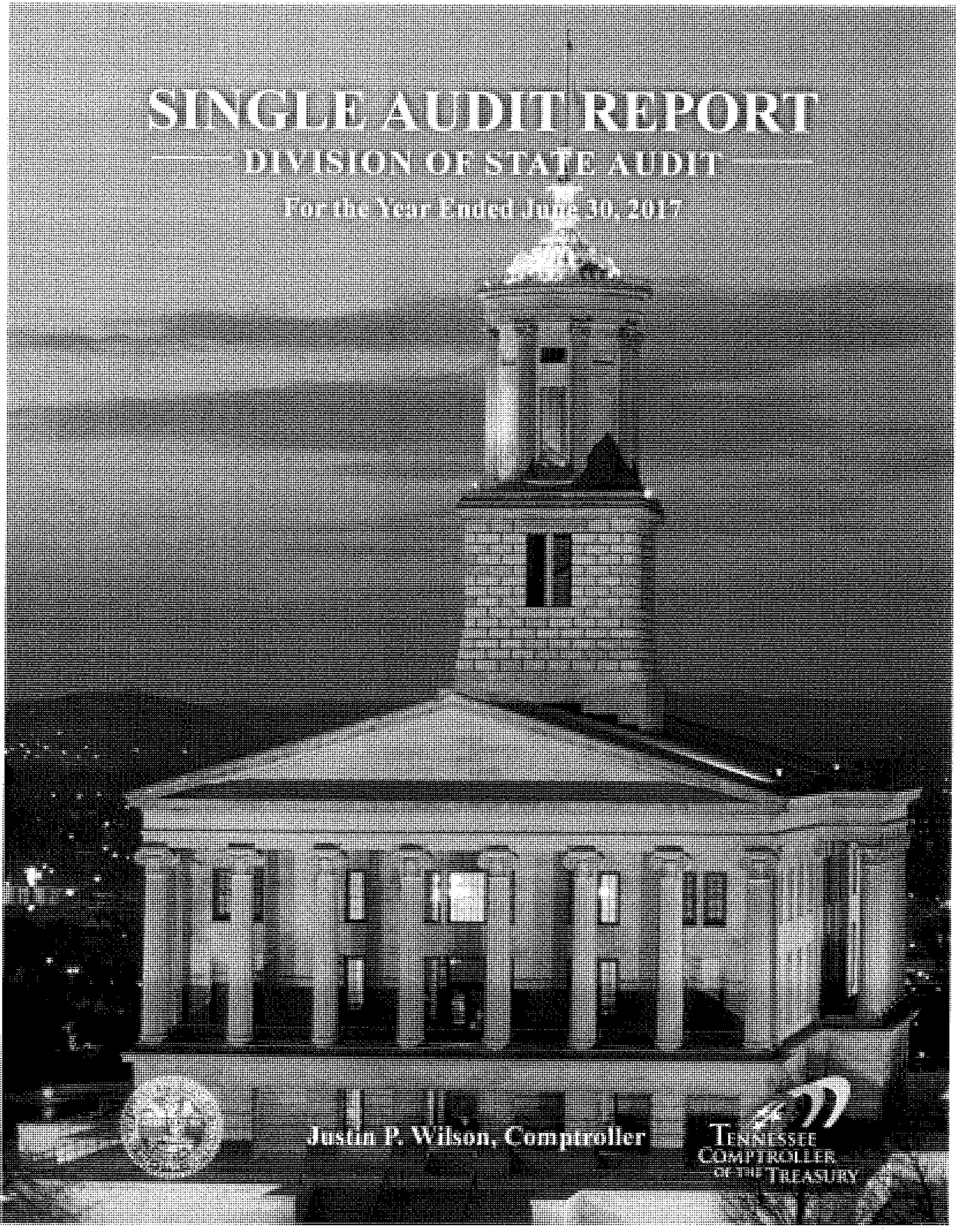
Brian J. Boon, Ph.D.
President/CEO

Enclosures

SINGLE AUDIT REPORT

DIVISION OF STATE AUDIT

For the Year Ended June 30, 2017



Justin P. Wilson, Comptroller

TENNESSEE COMPTROLLER OF THE TREASURY

TENNESSEE COMPTROLLER OF THE TREASURY

JUSTIN P. WILSON
Comptroller

JASON E. MUMPOWER
Chief of Staff

March 27, 2018

The Honorable Bill Haslam, Governor
Members of the General Assembly

Ladies and Gentlemen:

We are pleased to submit the thirty-fourth *Single Audit Report* for the State of Tennessee. This report covers the year ended June 30, 2017. The audit was conducted in accordance with the requirements of the Single Audit Act Amendments of 1996 and the provisions of Title 2, *Code of Federal Regulations*, Part 200, "Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards" (Uniform Guidance).

This *Single Audit Report* reflects federal expenditures of over $14.1 billion. We noted instances of noncompliance that resulted in qualified opinions on compliance for 2 of the state's 18 major federal programs. In addition, we noted other instances of noncompliance that meet the reporting criteria contained in the Uniform Guidance. We also noted material weaknesses and significant deficiencies in internal control over compliance with requirements related to federal programs. The instances of noncompliance, material weaknesses, and significant deficiencies related to federal programs are described in Section III of the Schedule of Findings and Questioned Costs.

The *Comprehensive Annual Financial Report* of the State of Tennessee for the year ended June 30, 2017, has been issued under a separate cover. In accordance with the standards applicable to financial audits contained in generally accepted government auditing standards, we are issuing our report on our consideration of the State of Tennessee's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts, and grants and other matters. We noted no material weaknesses in internal control. We noted no instances of noncompliance that we considered to be material to the state's basic financial statements.

We would like to express our appreciation to the Department of Finance and Administration and other state agencies, universities, and community colleges, for their assistance and cooperation in the single audit process.

Sincerely,

Deborah V. Loveless

Deborah V. Loveless, CPA, Director
Division of State Audit

State of Tennessee
Single Audit Report
For the Year Ended June 30, 2017

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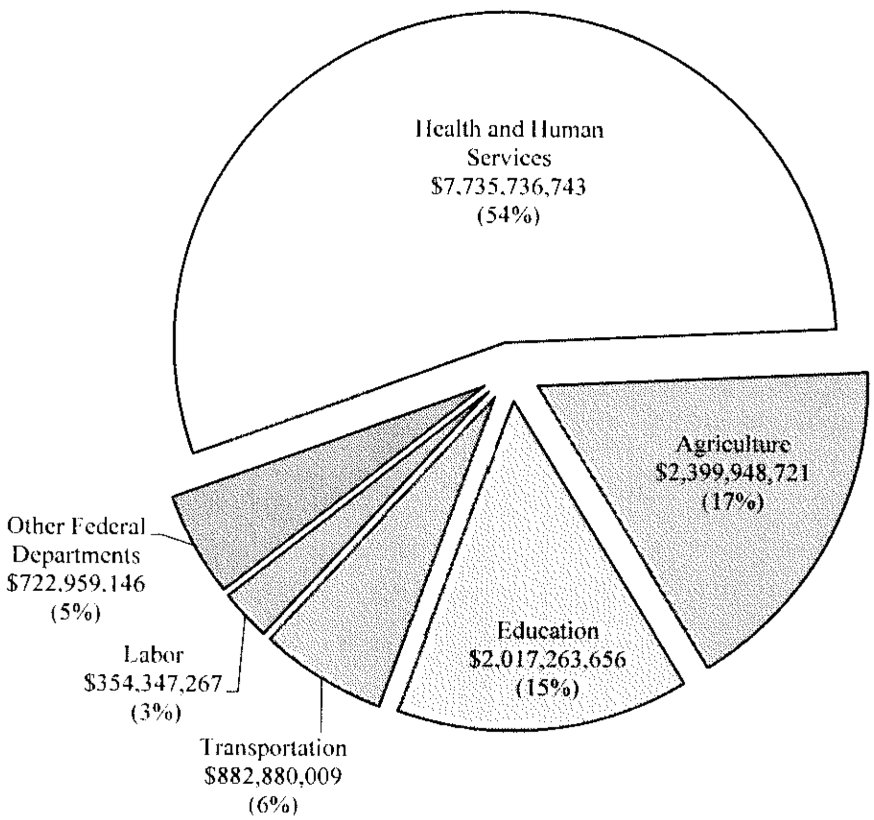
Expenditures by Awarding Agency
July 1, 2016, through June 30, 2017



State of Tennessee
Schedule of Findings and Questioned Costs
For the Year Ended June 30, 2017

Section I – Summary of Auditor's Results

Financial Statements

- We issued unmodified opinions on the basic financial statements.
- We identified no material weaknesses in internal control over financial reporting.
- No significant deficiencies in internal control over financial reporting were reported.
- We noted no instances of noncompliance considered to be material to the basic financial statements.

Federal Awards

- We identified material weaknesses in internal control over major programs.
- We identified significant deficiencies in internal control over major programs.
- We issued qualified opinions for CFDA 10.558 Child and Adult Care Food Program and the Child Care and Development Fund (CCDF) Cluster. We issued unmodified opinions for each of the other major federal programs.
- We disclosed audit findings that are required to be reported in accordance with 2 CFR 200.516(a).
- The dollar threshold used to distinguish between Type A and Type B programs, as prescribed in 2 CFR 200.518(b), was $30,000,000.
- The State of Tennessee does not qualify as a low-risk auditee under the provisions of 2 CFR 200.520.

State of Tennessee
Schedule of Findings and Questioned Costs
For the Year Ended June 30, 2017

Section I – Summary of Auditor's Results (continued)

CFDA Number	Name of Major Federal Program or Cluster
10.558	Child and Adult Care Food Program
17.225	Unemployment Insurance
84.002	Adult Education - Basic Grants to States
84.126	Rehabilitation Services - Vocational Rehabilitation Grants to States
84.287	Twenty-First Century Community Learning Centers
84.377	School Improvement Grants
93.563	Child Support Enforcement
93.568	Low-Income Home Energy Assistance
93.767	Children's Health Insurance Program
93.959	Block Grants for Prevention and Treatment of Substance Abuse
-	Supplemental Nutrition Assistance Program (SNAP) Cluster
-	Child Nutrition Cluster
-	Housing Voucher Cluster
-	Clean Water State Revolving Fund Cluster
-	Student Financial Assistance Cluster
-	Temporary Assistance for Needy Families (TANF) Cluster
-	Child Care and Development Fund (CCDF) Cluster
-	Medicaid Cluster

Finding Number	2017-010
CFDA Number	10.559, 10.560, 10.561, 84.126, 93.558, 93.563, 93.575, 93,778, and 96.001
Program Name	Child Nutrition Cluster State Administrative Expenses for Child Nutrition Supplemental Nutrition Assistance Program Cluster Rehabilitation Services - Vocational Rehabilitation Grants to States Temporary Assistance for Needy Families Cluster Child Support Enforcement Child Care and Development Fund Cluster Medicaid Cluster Disability Insurance/Supplemental Security Income Cluster
Federal Agency	Department of Agriculture Department of Education Department of Health and Human Services Social Security Administration
State Agency	Department of Human Services
Federal Award Identification Number	201616N109945, 201717N109945, 201717N253345, 201616IS251445, 201717IS251445, 8044 H126A160063, 8044 H126A170063, G1502TNTANF, G1602TNTANF, 1504TNCSES, 1604TNCSES, 1704TNCSES, G1601TNCCDF, G1701TNCCDF, 05-1605TN5ADM, 05-1705TN5ADM, 8826 04-16-04TNDI00, and 8826 04-17-04TNDI00
Federal Award Year	2015 through 2017
Finding Type	Significant Deficiency (10.559, 10.561, 84.126, 93.563, and 93.575) Material Weakness (93.558) Noncompliance
Compliance Requirement	Allowable Costs/Cost Principles
Repeat Finding	2016-015
Pass-Through Entity	N/A

Questioned Costs

CFDA	Federal Award Identification Number	Amount
10.560	201717N253345	$6,623
10.561	201616IS251445	($79,754)
10.561	201717IS251445	$164,918
93.563	1504TNCSES	($6,189)
93.563	1604TNCSES	($242)
93.563	1704TNCSES	$57,894
93.778	05-1605TN5ADM	($44,191)
93.778	05-1705TN5ADM	$113,510
96.001	8826 04-16-04TNDI00	($41)
96.001	8826 04-17-04TNDI00	$123,359

As noted in the prior audit, fiscal staff for the Department of Human Services again did not adhere to federal requirements by allocating costs to programs based on prior period information rather than current period information, resulting in federal questioned costs of $335,887

Background

Because the Department of Human Services administers various public assistance programs, federal regulations require the state to submit a cost allocation plan that outlines the procedures used to identify, measure, and allocate costs to all programs administered by the department. Fiscal staff within the Department of Finance and Administration create and submit the cost allocation plan on behalf of the Department of Human Services, as well as allocate costs to federal grant awards in accordance with the cost allocation plan.

In accordance with federal regulations, fiscal staff allocate administrative costs that cannot be directly charged to a specific federal program to all benefitting federal programs based on the cost allocation plan. During the audit period, July 1, 2016, through June 30, 2017, two cost allocation plans were effective for the department. The first plan was effective July 1, 2016, through March 31, 2017. The second was effective April 1, 2017. A total of $381,213,289 of the department's expenditures during our audit period was subject to allocation under the cost allocation plan. (Federal regulations exclude from cost allocation plans expenditures for financial assistance, medical vendor payments, food stamps, and payments for services and goods provided directly to program recipients.)

According to Title 45, *Code of Federal Regulations*, Part 95, Section 507(a), a cost allocation plan for a state agency must describe the procedures used to identify, measure, and allocate all costs to each of the programs operated by the state agency.

Each quarter, fiscal staff prepare cost allocation tables. Generally, each table covers a specific activity that department staff perform for programs, identifies one or more federal programs to which costs for the activity should be charged, and identifies the percentage of costs associated with the specific activity that should be charged to each federal program.

Fiscal staff then use the cost allocation tables' percentages to prepare cost allocation spreadsheets that identify the amount of expenditures that fiscal staff should allocate to the federal programs administered by the department.

Finally, fiscal staff enter cost allocation entries into the department's accounting system based on the cost allocation calculations documented in the spreadsheets.

Percentages Used to Allocate Costs

For the department's activities that benefit multiple federal and state programs, fiscal staff[6] allocate the total amount of expenditures for the activities to the programs based on percentages.

To describe fiscal staff's responsibilities under cost allocation, for example, in January, if 75% of the department's employees work on the Supplemental Nutrition Assistance Program (SNAP) and 25% work on the Temporary Assistance for Needy Families (TANF) program, fiscal staff should allocate costs for the Commissioner's Office, which oversees all employees, 75% to SNAP and 25% to TANF. We continue this example for the next month under the assumption that in February a different proportion of employees work on these federal programs. Thus, in February, if 60% of the department's employees work on SNAP and 40% work on TANF, federal cost principles require allocating the expenditures to the grants based on February's 60/40 percentages, rather than the prior period's 75/25 percentages. We found, however, that fiscal staff did not always use current period percentages, and regularly used the prior period's percentages.

To understand management's rationale for this methodology, we discussed the process with the Department Controller, who stated that he believed that using prior period percentages would not over- or undercharge programs.[7] We noted, however, that using prior period percentages did not adhere to a several of federal requirements. For example, $109,884,675 of the department's administrative costs incurred during the audit period, July 1, 2016, through June 30, 2017, was allocated using random moment time sampling, and Title 2, *Code of Federal Regulations* (CFR), Part 200, Section 430(i)(5)(i)(C), requires the results of the state's random moment sampling method to be applied to the period being sampled. While additional specific requirements are addressed further below, the basic cost principle is that federal regulations require costs to be allocated to federal programs based on the relative benefit received. In the example discussed above, SNAP only received 60% of the benefits in February; therefore, allocating costs to SNAP based on the prior period percentage (75%) would overcharge SNAP by 15%.

Even if the prior period's percentages are consistently used each month instead of the current period's percentages, programs could be over- or undercharged. These differences can accumulate over time, as demonstrated by the $188,302 total overcharge for Medicaid in the example in Table 1 below, which uses actual data for the Adult Protective Services division of the department for July 2016 through March 2017:

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[6] On April 11, 2016, the Department of Finance and Administration assumed responsibility for performing the Department of Human Services' fiscal functions, including preparing and implementing cost allocation plans. Therefore, the Department Controller and other fiscal employees referenced in this finding are employees within the Department of Finance and Administration.

[7] As discussed further below, we could find no evidence to support the conclusion that programs would not be over- or undercharged by using prior period information, and the evidence we reviewed suggested the opposite.

Table 1
Example of Accumulating Overcharges and Undercharges
Caused by Using Prior Period Percentages for Cost Allocation Table ACS-3*

Period	Program	Current Period's Percentage	Prior Period's Percentage	Percentage Difference	Allocable Costs	SSBG Overcharge (Undercharge)	Medicaid Overcharge (Undercharge)
July – Sep 2016	SSBG	61%	59%	-2%	$2,283,194	$(53,621)	
July – Sep 2016	Medicaid	39%	41%	2%	$2,283,194		$53,621
Oct – Dec 2016	SSBG	64%	61%	-3%	$2,355,050	$(72,179)	
Oct – Dec 2016	Medicaid	36%	39%	3%	$2,355,050		$72,179
Jan – Mar 2017	SSBG	67%	64%	-2%	$2,569,663	$(62,502)	
Jan – Mar 2017	Medicaid	33%	36%	2%	$2,569,663		$62,502
					Grand Total	**$(188,302)**	**$188,302**

* Percentages in this table were rounded for presentation in the percentage columns, but not rounded in the calculations in the difference and overcharge (undercharge) columns.

Based on our review of the department's accounting records, the department allocated $381,213,289 through the cost allocation process during the audit period, July 1, 2016, through June 30, 2017; therefore, it is critical that the percentages of costs allocated to various programs are appropriate, because small differences in prior period and current period percentages could lead to fiscal staff overcharging federal programs by significant amounts over time.

Audit Results

During the prior audit, we noted that fiscal staff used prior period percentages to allocate costs for two divisions within the department, among other instances of noncompliance related to the cost allocation plan. Management concurred in part with the prior audit finding and noted that the department was in the process of revising the cost allocation plan to take effect April 1, 2017.

During the current audit, we again noted several instances in which the department used prior period information to allocate the current period's costs for certain divisions during the period July 1, 2016, through March 31, 2017. In addition, the department amended its cost allocation plan, effective April 1, 2017, to begin allocating *all* divisions' costs based on prior period percentages. As a result of the errors identified during the audit, we questioned a net[8] total of $335,887 in federal costs and $180,994 in state matching costs.

Summary of Conditions

We tested the department's cost allocation processes for the periods October 1, 2016, to December 31, 2016, and April 1, 2017, to June 30, 2017. Based on testwork performed, we found that the Department Controller did not ensure that fiscal staff allocated costs in accordance with federal requirements. Specifically, we noted that fiscal staff

[8] Due to the nature of the cost allocation process, errors generally result in overcharging certain federal programs and undercharging others. After netting overcharges against any undercharges for the same federal program, we questioned the net amount by which each federal program was overcharged.

- used allocation information from the prior quarter (prior period percentages) to allocate all costs for the department for the quarter April 1, 2017, through June 30, 2017 (Condition A);
- used prior period percentages to allocate certain divisions' costs for part or all of the audit period, July 1, 2016, through June 30, 2017 (Condition B).

Condition A. Fiscal Staff Allocated All Departmental Costs Using Prior Period Percentages for Three Months

Throughout our audit fieldwork we discussed management's actions since the prior audit to resolve the prior audit issues. We recognize, based on these discussions, that management is continuing to work through their processes to find the best method to achieve federal compliance given the magnitude of the transactions involved in administering the federal grants. As auditors, we are also required to follow federal regulations in performing our audit and in reporting our conclusions. In this audit, given management's on-going assessment and efforts to change processes to resolve all prior noted conditions, we believe it is important to note that our finding is required since full corrective action has not yet occurred. The next audit cycle will be a critical analysis of true resolution. As such, during our audit scope we found the following condition.

The department's amended *Public Assistance Cost Allocation Plan* became effective on April 1, 2017. During the planning stage of the audit, we noted that the Department Controller included language in the plan that stated that "the Department generally relies on allocation statistics from the immediately preceding quarter [prior period percentages] to allocate current quarter costs." This means that for the period April 1, 2017, through June 30, 2017, fiscal staff allocated all costs based on the relative benefits federal programs received in the prior quarter, January 1, 2017, through March 31, 2017.

Based on discussion with the U.S. Department of Health and Human Services' Cost Allocation Services Division (CAS), using prior quarter percentages was appropriate for estimates, but the department would need to perform end of the year adjustments using current quarter data for each quarter. CAS stated if fiscal staff did not make these adjustments, the department would not be in compliance with 2 CFR 200.405(a).

In our discussions with the Department Controller, he asserted that the differences caused by using prior quarter percentages would be negated in the next quarter when the current quarter's percentages will be used. Similarly, in an email exchange between the Department Controller and a federal official involved in the cost allocation approval process—the Lead Grants Management Specialist within the U.S. Department of Health and Human Services' Administration for Children and Families—the Department Controller provided information to the federal official, such as,

> By consistently using the same methodology from quarter to quarter, the methodology does not over/under allocate costs to any benefiting program. . . . In short, there is nothing to "true up." At worst, were the allocation statistics to fluctuate significantly from one quarter to the next, there would be a one quarter "lag" in reflecting under/over allocations that would be compensated for in the subsequent quarter.

Although the federal official voiced her concerns regarding the methodology by stating, in part, "the methodology could under/over allocate costs to benefitting programs which is why ACF [Administration for Children and Families] requests a 'true up' once all statistics are intact," the Department Controller responded by stating, in part, "it would be at worst one more quarter before those allocation statistics were used to allocate current quarter costs; therefore, 'truing them up' for the fluctuation."

In our attempt to determine whether management's statements to the federal partner were reasonable, we asked for supporting evidence of management's cost impact analysis. Because this analysis did not include all divisions of the department and only involved one quarter, we did not think the analysis was sufficient to support the assertion that the department's methodology would achieve compliance over two quarters. Management provided no other evidence to support management's statements.

In an effort to satisfy ourselves as to whether the methodology based on prior period percentages, rather than current period percentages, was a reasonable methodology, we performed a comprehensive analysis to test management's statement that overcharges caused by using prior period percentages would reverse in the subsequent period. Specifically, for all divisions in the department, we reperformed the department's cost allocation procedures using prior period percentages for the period October 1, 2016, through March 31, 2017. We then compared these allocations to the fiscal staff's actual calculations, which used current quarter percentages for the same period of time. It is important to note that our calculations were based on fiscal staff's own schedules; we simply substituted fiscal staff's current quarter percentages with their prior quarter percentages in their schedules and summarized the results. Based on our procedures, we found that the differences caused by using prior period data did not reverse in the next quarter and the differences this methodology would cause over time did not appear to be immaterial as indicated by management.

Specifically, we noted that using prior period percentages would have resulted in federal programs being overcharged by up to $500,000 per program over the six-month period, which suggests that using the methodology could result in overcharging programs by up to $1 million per year. It is not clear that federal officials would consider potential overcharges of up to $1 million per program per year to be immaterial. See Table 2 below for the differences using prior period percentages would have caused each quarter over the course of these two periods.

Table 2
Overcharges (Undercharges) by Program Due to the Use of Prior Period Statistical Data, for the Period October 1, 2016, through March 31, 2017

Program	October 2016 - December 2016	January 2017 - March 2017	Total Expenditures
Programs Overcharged			
Child Care and Development Block Grant	$53,234	$142,165	$195,399
Child Support Enforcement	(47,688)	113,691	66,003
Community Services Block Grant	90,580	(28,467)	62,113

Medical Assistance Program	105,767	1,583	107,350
State Administrative Expenses for Child Nutrition	(46,188)	136,680	90,492
Social Security Disability Insurance	39,904	34,375	74,279
Temporary Assistance for Needy Families	237,513	293,543	531,056
Totals	**$433,122**	**$693,570**	**$1,126,692***
Programs Undercharged			
State Only Activities	$11,864	(108,333)	(96,469)
Child and Adult Care Food Program	5,228	(104,297)	(99,069)
Independent Living Services for Older Individuals Who Are Blind	(4,565)	2,969	(1,596)
Summer Food Service Program	(56,441)	(3,399)	(59,840)
Supplemental Nutrition Assistance Program	(222,942)	(372,362)	(595,304)
Social Services Block Grant	(116,816)	(80,794)	(197,610)
Vocational Rehabilitation	(49,579)	(30,255)	(79,834)
Totals	**$(433,251)**	**$(696,471)**	**$(1,129,722)***

*There is a net total of ($3,032) due to immaterial errors detected in fiscal staff's original calculations, as well as rounding differences in our calculations.

Because federal requirements, communications from federal officials, and our procedures all suggested that using current period percentages was the appropriate method, we reperformed the cost allocation procedures for the period April 1, 2017, through June 30, 2017, using current period percentages and compared these allocation amounts to the amounts fiscal staff calculated using prior period percentages. We questioned the differences caused by using prior period data rather than current period data. See Table 3 below for more information.

Table 3
Overcharges (Undercharges) by Program Due to the Use of Prior Period Percentages for the Period of April 1, 2017, Through June 30, 2017

Program	Federal Expenditures	State Expenditures	Total Expenditures
Programs Overcharged			
Child Support Enforcement	$45,761	$23,574	$69,335
Medical Assistance Program	44,087	44,087	88,174
State Administrative Expenses for Child Nutrition	7,182	-	7,182
Summer Food Service Program	1	-	1
Supplemental Nutrition Assistance Program	192,586	192,586	385,172
Social Security Disability Insurance	123,359	-	123,359
Total	**$412,976**	**$260,247**	**$673,223***
Programs Undercharged			
Child Care and Development Block Grant	$(7,474)	$(130,477)	$(137,951)

Community Services Block Grant	(6,873)	-	(6,873)
Independent Living Services for Older Individuals Who Are Blind	(7,256)	(806)	(8,062)
Social Services Block Grant	(48,484)	-	(48,484)
Temporary Assistance for Needy Families	(200,954)	(200,954)	(401,908)
Vocational Rehabilitation	(55,002)	(14,886)	(69,888)
Total	**$(326,043)**	**$(347,123)**	**$(673,166)***

*The sum of all overcharges and undercharges due to using prior period percentages should be zero. The sum of overcharges and undercharges in the table above is $57 due to immaterial errors detected in fiscal staff's original calculations, as well as rounding differences in our calculations.

It is important to note that our analyses of the two plans in effect for our audit scope (the new cost allocation plan on April 1, 2017, and the plan for October 1, 2016, through March 31, 2017) are not directly comparable because the plans allocate costs differently. Tables 2 and 3 are stand-alone conclusions. More specifically, the April 1, 2017, plan introduced a variety of changes, such as changes from direct to indirect allocation methodologies, changes to cost allocation bases, eliminating cost pools and merging them with pre-existing ones, and more. Therefore, the factors that caused the differences identified in Tables 2 and 3 are not necessarily identical.[9]

As a result, even though some programs' cumulative differences would be reduced if all three quarters' results were added together, adding the quarters together would not be appropriate as the allocation methodologies were not consistent. Additionally, some programs' cumulative differences would continue to increase if the quarters were added together.

After we performed the comprehensive analysis in December 2017, we learned that the federal government had approved the April 1, 2017, cost allocation plan in which management stated they planned to use prior period percentages. According to the approval letter, dated December 5, 2017,

> Approval of the plan/amendment cited above is predicated upon conditions that . . . (4) the approval is based on information provided by the State and is void if the information is later found to be materially incomplete or inaccurate (5) the allocation methods proposed result in an equitable distribution of costs to programs.

As described above, we noted that the Department Controller had informed federal officials that the use of prior period percentages "does not over/under allocate costs to any benefiting program". However, because of the inconsistencies between management's statements and our analysis, we are not able to conclude that fiscal staff adhered to condition 4 referenced above. In addition, based on our audit procedures described above, the allocation methods used by the department did not result in an equitable distribution of costs to programs, which does not comply with condition 5 above. Further, according to decisions by the U.S. Department of Health and Human Services' Departmental Appeals Board, such as decision Number 370, issued in December 1982, the board has repeatedly found that ". . . an approved CAP [Cost Allocation Plan] does not constitute prior

[9] Although the factors that caused the differences identified in Tables 2 and 3 are not necessarily identical, the October 1, 2016, through March 31, 2017, analysis provides evidence supporting the general conclusion that using prior period information rather than current period information can result in differences that may accumulate and become significant over time, and we identified no evidence to suggest that this general conclusion was not applicable to the April 1, 2017, plan.

approval to deviate from applicable statutes and regulations." Finally, in our communications with federal officials and our review of correspondence between federal officials and management, the officials consistently communicated that allocating costs based on prior period percentages without subsequent adjustment was not appropriate. Due to all these factors, and given we cannot yet audit management's intentions to adjust the estimates to actual, we included this matter as an audit finding despite the federal government's approval of the plan.

We also noted that using prior period information led to fiscal staff allocating approximately $3.4 million in expenditures that was not based on valid statistical data, which is not in accordance with federal requirements. See finding 2017-011 for more information.

Cause for Condition A

The primary reason fiscal staff moved to allocating costs based on prior period percentages was so that fiscal staff could complete the cost allocation process more quickly after the end of each quarter. The Department Controller noted that the department had prior audit findings related to cost allocations not being adjusted to actual timely in accordance with an agreement between the state and the federal government related to cash management (the Treasury-State Agreement). We noted, however, that management could have pursued other options to improve the timeliness of adjustments, such as amending the agreement to extend the deadline for making cost allocation entries or streamlining fiscal processes for preparing cost allocation schedules. In addition, we noted that the time constraints also appeared to be due to some extent to a lack of sufficient staff. Specifically, only two fiscal staff appeared to be primarily responsible for performing the entire cost allocation process (one person prepared the percentages, and another applied the percentages to costs).

Another contributing factor was the Department Controller's belief that using prior period percentages would not lead to overcharging or undercharging federal programs if applied consistently over time; however, our testwork did not support this statement.

Condition B. Fiscal Staff Used Prior Period Percentages to Allocate Certain Divisions' Costs for Part or All of the Audit Period

Condition A above is related to a formal accounting practice established in the department's cost allocation plan for allocating the entire department's costs using prior period information beginning April 1, 2017; however, we also identified isolated situations in which fiscal staff used prior period percentages for certain departmental divisions. These issues primarily occurred between July 1, 2016, and March 31, 2017, prior to the new cost allocation plan taking effect. See the table below for additional information.

Table 4
Allocations of Costs Using Prior Period Percentages by Division and Time Period

Divisions	Allocation Basis	Time Period of Costs	Time Period of Percentages Used to Allocate Costs
APS, FA1, FA2, FO, INV*	Random Moment Sampling	July 2016 and August 2016	April 2016 through June 2016
Family Assistance	Various	October 2016 through December 2016	September 2016
Appeals and Hearings	Case Counts	October 2016 through December 2016	September 2016
Office of General Counsel	Workload Hours	July 2016 through June 2017	June 2016 through May 2017

*APS – Adult Protective Services
FA1 – Family Assistance – Field Staff, Management, and Support Staff
FA2 – Family Assistance – Hospital-Based Eligibility Determination Workers
FO – Family Assistance – Field Operations
INV – Investigations

For all divisions identified in the table above except for the Office of General Counsel, we calculated the correct allocation of costs using the correct percentages for the applicable time period and compared our results to fiscal staff's calculations based on prior period percentages. We questioned the differences between our calculations and the amounts allocated by fiscal staff. See Table 5 below for the amount of overcharges and undercharges by program. For the Office of General Counsel, we did not question the costs related to this issue because the data needed to calculate these costs was not readily available in the department's accounting system.

Table 5
Programs Overcharged (Undercharged) Due to Allocating Costs Based on Prior Period Percentages

Program	Federal Expenditures	State Expenditures	Total Expenditures
Programs Overcharged			
Child Care and Development Block Grant	$1,590	$48,791	$50,381
Child Support Enforcement	5,702	2,937	8,639
Medical Assistance Program	25,232	25,232	50,464
Temporary Assistance for Needy Families	18,662	119,221	137,883
Vocational Rehabilitation	372	101	473
Total	**$51,558**	**$196,282**	**$247,840**
Programs Undercharged			
Social Security Disability Insurance	$(41)	-	$(41)
Social Services Block Grant	(31,231)	-	(31,231)
State Administrative Expenses for Child Nutrition	(559)	-	(559)
Summer Food Service Program	(1,165)	-	(1,165)

Supplemental Nutrition Assistance Program	(107,422)	(107,422)	(214,844)
Total	**$(140,418)**	**$(107,422)**	**$(247,840)**

Source: Summarized using accounting records from Edison, the state's accounting system, and the department's cost allocation schedules.

After we brought this matter to the attention of fiscal staff, fiscal staff partially resolved the errors identified in Table 5 above by correcting the cost allocation calculations for two divisions, Family Assistance and Appeals and Hearings, for the October through December 2016 costs that were allocated improperly.

Cause for Condition B

For the Family Assistance and Appeals and Hearings divisions for the period October through December 2016, the errors noted in Table 5 above were due to fiscal staff accidentally failing to replace the prior period cost allocation tables with the current tables when preparing the cost allocation spreadsheets. For the remainder of the divisions and time periods in Table 3 above, when these errors occurred, it does not appear that fiscal staff were aware that the cost allocation tables should not be created using prior period percentages.

Condition C. Risk Assessment

Given the problems identified during our fieldwork, we also reviewed the department's November 2016 Financial Integrity Act Risk Assessment and determined that top management assessed the risk that "Costs charged to a federal program are not allowable under program regulations" as having a remote likelihood and small impact; however, management did not identify any mitigating controls related to the issue. Given the unallowable costs and cost principles issues identified in this finding and others during the current audit, such as 2017-015, 2017-033, and 2017-037, we concluded that management should have assessed the likelihood as reasonably possible, assessed the impact as large, and included a control activity to mitigate the risk in the department's annual risk assessment.

Criteria for All Conditions

According to *A Guide for State, Local and Indian Tribal Governments – Cost Allocation Principles and Procedures for Developing Cost Allocation Plans* (ASMB C-10), Section 3-23, prior periods' random moment time sampling percentages and other time and effort percentages may not be used to allocate the current period's costs:

> **Can the results of an acceptable statistical sampling method or time and effort reporting covering one period of time be applied to a different period, e.g., a prior quarter? [Att. B, ¶ 11.h(5)(c)]**
>
> No. The results of a specific period represents the values experienced during that period only. Attachment B, paragraph 11.h(5)(c) requires that time and effort reporting coincide with one or more pay periods. Therefore, retroactive application of such results, whether they are statistically based or effort reporting, is unacceptable. However, prior period actuals may be used as estimates for applying

costs in a future period, provided that the estimates are adjusted back to actual effort for that period when claimed for reimbursement.

The guide quoted above has the effect of a regulatory requirement because it represents instructions released by the Department of Health and Human Services, and 45 CFR 95.507(a)(2) requires the cost allocation plan to "Conform to the accounting principles and standards prescribed in Office of Management and Budget Circular A-87, and other pertinent Department regulations and instructions."

Like ASMB C-10, 2 CFR 200.430(i)(5)(i)(C) also requires the results of the state's random moment sampling method to be applied to the period being sampled.

According to OMB Circular A-87, "Cost Principles for State, Local and Indian Tribal Governments," Attachment A, Section C.3.a-b, a cost is allocable to a particular federal award or other cost objective if the goods or services involved are chargeable or assignable to that federal award or cost objective in accordance with relative benefits received, and all activities which benefit from indirect costs will receive an appropriate allocation of indirect costs. These requirements are also stated in 2 CFR 200.405(a-b).

For direct costs, 2 CFR 200.405(d) states that if a cost benefits two or more projects or activities in proportions that can be determined without undue effort or cost, the cost must be allocated to the projects based on the proportional benefit.

Effect for All Conditions

Failure to allocate costs in accordance with the cost allocation plan and federal requirements increases the risk that fiscal staff will fail to assign an appropriate share of costs to programs and that federal grantors will disallow costs charged to federal programs.

Additionally, federal regulations address actions that federal agencies may impose in cases of noncompliance. As noted in 2 CFR 200.338, "If a non-Federal entity fails to comply with Federal statutes, regulations or the terms and conditions of a Federal award, the Federal awarding agency or pass-through entity may impose additional conditions," including, as described in Section 200.207, "Specific conditions":

(1) Requiring payments as reimbursements rather than advance payments;

(2) Withholding authority to proceed to the next phase until receipt of evidence of acceptable performance within a given period of performance;

(3) Requiring additional, more detailed financial reports;

(4) Requiring additional project monitoring;

(5) Requiring the non-Federal entity to obtain technical or management assistance; or

(6) Establishing additional prior approvals.

Furthermore, Section 200.338 also states, If the Federal awarding agency or pass-through entity determines that noncompliance cannot be remedied by imposing additional conditions [as described above], the Federal awarding agency or pass-through entity may take one or more of the following actions, as appropriate in the circumstances:

(a) Temporarily withhold cash payments pending correction of the deficiency by the non-Federal entity or more severe enforcement action by the Federal awarding agency or pass-through entity.

(b) Disallow (that is, deny both use of funds and any applicable matching credit for) all or part of the cost of the activity or action not in compliance.

(c) Wholly or partly suspend or terminate the Federal award.

(d) Initiate suspension or debarment proceedings as authorized under 2 CFR part 180 and Federal awarding agency regulations (or in the case of a pass-through entity, recommend such a proceeding be initiated by a Federal awarding agency).

(e) Withhold further Federal awards for the project or program.

(f) Take other remedies that may be legally available.

Questioned Costs

We questioned a total of $516,881 due to the net amount of overcharges to federal programs, consisting of federal questioned costs of $335,887 and $180,994 in questioned costs related to state matching funds for federal grant awards. See Table 6 for details regarding all overcharges and undercharges.

Table 6
Total Questioned Costs by Federal Program

Program	Federal Expenditures	State Expenditures	Total Expenditures
Programs Overcharged			
Child Support Enforcement	$51,463	$26,511	$77,974
Medical Assistance Program	69,319	69,319	138,638
State Administrative Expenses for Child Nutrition	6,623	-	6,623
Supplemental Nutrition Assistance Program	85,164	85,164	170,328
Social Security Disability Insurance	123,318	-	123,318
Total	**$335,887**	**$180,994**	**$516,881**
Programs Undercharged			
Child Care and Development Block Grant	$(5,884)	$(81,686)	$(87,570)
Community Services Block Grant	(6,873)	-	(6,873)
Independent Living Services for Older Individuals Who Are Blind	(7,256)	(806)	(8,062)

Summer Food Service Program	(1,164)	-	(1,164)
Social Services Block Grant	(79,715)	-	(79,715)
Temporary Assistance for Needy Families	(182,292)	(81,733)	(264,025)
Vocational Rehabilitation	(54,630)	(14,785)	(69,415)
Total	**$(337,814)**	**$(179,010)**	**$(516,824)**

Concerning questioned costs, 2 CFR 200.516(a)(3) requires us to report known questioned costs that are greater than $25,000 for a type of compliance requirement for a major program.

In addition, 2 CFR 200.516(a)(4) requires us to report known questioned costs that are greater than $25,000 for a federal program which is not audited as a major program. This finding, in conjunction with findings 2017-12, 2017-014, and 2017-015, results in total known federal questioned costs exceeding $25,000 for a federal program which is not audited as a major program.

According to 2 CFR 200.84,

> *Questioned cost* means a cost that is questioned by the auditor because of an audit finding:
>
> (a) Which resulted from a violation or possible violation of a statute, regulation, or the terms and conditions of a Federal award, including for funds used to match Federal funds;
>
> (b) Where the costs, at the time of the audit, are not supported by adequate documentation; or
>
> (c) Where the costs incurred appear unreasonable and do not reflect the actions a prudent person would take in the circumstances.

Recommendation

The Commissioner of the Department of Finance and Administration (the Commissioner) should ensure that proposed revisions to cost allocation plans are supported by comprehensive estimated cost analyses that span multiple time periods, and should establish adequate internal controls to ensure that communications to federal officials regarding the impact of proposed changes are supported by these impact analyses. These controls should include ensuring that the communications are documented and distributed to the relevant fiscal staff.

In order to allow fiscal staff to complete cost allocation entries timely without using prior period information, the Department Controller, in consultation with appropriate officials within the Department of Finance and Administration, should consider alternatives for ensuring that cost allocation entries are performed more quickly, such as

- updating the Treasury-State Agreement with the U.S. Department of Treasury to extend the amount of time fiscal staff have to perform cost allocation entries;
- hiring or reassigning additional staff to assist in the cost allocation process; and

- discussing with Comptroller's Office staff potential automation solutions for cost allocation processes using the department's existing spreadsheet tools, including strategies for automatically detecting when fiscal staff have accidentally allocated costs based on prior period percentages.

The Commissioner of the Department of Human Services should assess all significant risks with sufficient attention to the impact and likelihood of the risk. The risk assessment and the mitigating controls should be adequately documented and approved by the Commissioner, who should implement effective controls to ensure compliance with applicable requirements, assign employees to be responsible for ongoing monitoring of the risks and any mitigating controls, and take action if deficiencies occur.

Management's Comment

We concur in part.

Condition A. Fiscal Staff Allocated All Departmental Costs Using Prior Period Percentages for Three Months

The department does not concur. A cost allocation plan is a narrative of the procedures that the department will use in identifying, measuring, and allocating all department costs incurred in support of all programs administered or supervised by the department. The plan utilizing the methodology described in condition A was approved by Cost Allocation Services within the U.S. Department of Health and Human Services even after being contacted by the state auditor who voiced concerns with the approach.

In addition, management discussed the concept of using prior quarter percentages extensively with its federal partners while its April 1, 2017 effective public assistance cost allocation plan (PACAP) was being developed and reviewed for approval. This discussion resulted in valuable clarifications and understandings for all participants, and ultimately resulted in the following support for this approach being received from the Lead Grants Management Specialist, HHS/ACF/OA – Office of Grants Management:

> *ACF does not have issues with application of prior quarter statistics as long as appropriate quarter adjustments after subsequent analysis is completed. In our discussions, your intent to adhere to these guidelines is clear and subsequent PACAP submissions have been augmented to clarify this understanding.*

The department clearly documented in its subsequent July 1st cost allocation plan submission that it would periodically evaluate the differences between allocation approaches and make adjustments for any material variations.

Management does not believe the tables presented in this finding provide sufficient evidence that the allocation methods utilized by the department will not result in an equitable distribution of costs to programs. While table 2 and 3 do present three quarters of data, as noted in the finding, they are not comparable, so they provide little value in establishing whether or not allocations using the federally approved technique over an extended period are equitable.

Finally it is important to note, that as stated in the finding, management communicated to the state auditor that the primary reason behind the approach taken in the PACAP was to address other findings related to cost allocation timeliness. Management agrees that there are alternative approaches to addressing the timeliness issue, but does not believe that one is measurably preferable over another.

Condition B. Fiscal Staff Used Prior Period Percentages to Allocate Certain Divisions' Costs for Part or All of the Audit Period

The department concurs that the cost allocation plan in place did not adequately represent all departmental practices which is why the plan was amended effective April 1, 2017. Due to the time delay associated with compiling results from the Random Moment Sample (RMS), prior quarter RMS results were used in some instances so as not to delay the cost allocation process. This is another contributing factor to why the plan was amended as described in condition A.

As noted in the finding, cost allocations for Family Assistance and Appeals and Hearings were corrected. Costs for the Office of General Counsel were allocated in accordance with the approved cost allocation plan in place at the time.

Condition C. Risk Assessment

The department completes its annual risk assessment as required under *Tennessee Code Annotated*, Section 9-18-101 using guidance provided by the Tennessee Department of Finance and Administration (F&A). The Department's November 2016 Financial Integrity Act Risk Assessment risks of non-compliance were assessed by compliance type requirement for the Department as a whole. For the December 2017 Financial Integrity Act Risk Assessment, based on revised F&A guidance risks, were assessed on a more programmatic/divisional level.

Auditor's Comment

Condition A. Fiscal Staff Allocated All Departmental Costs Using Prior Period Percentages for Three Months

We are not aware of any relevant federal requirements that permit fiscal management to determine the materiality of overcharges to federal grants. We also have specific federal requirements which require us to report questioned costs when those costs exceed the federal reporting thresholds. As such we have reported the $516,881 in overcharges to federal programs for the quarter ended June 30, 2017, based on our requirement to do so.

It is also not clear that federal officials responsible for approving the plan were aware that fiscal management intends to only address variations deemed significant, instead of "truing up" all variations to actual. Specifically, the July 1st plan states, "Prior quarter adjustments will be made on Federal reports when appropriate." Based on discussion with fiscal management, "when appropriate" means when management concludes variations are material, but this was not explained in the plan or any other communication we reviewed. Without this clarity, there may be differing opinions between management, the federal partners, and the state auditors regarding materiality of variations.

As of March 2018, there was no indication that fiscal management had performed the periodic review described in management's comment for the quarter ended June 30, 2017, and fiscal management had not informed us of when this will occur. The cost principles identified in this finding do not authorize temporary noncompliance, and the state's Treasury-State agreement required cost allocations to be adjusted to actual quarterly. Further, the CAS official we spoke to indicated that allocations should be adjusted to actual each fiscal year, at least. As a result, we are required to report this issue until fiscal management has implemented a process that ultimately corrects these cost allocations. We look forward to working with management and the federal partners in the future to achieve an appropriate resolution to this matter.

Finding Number	2017-011
CFDA Number	10.558, 10.559, 10.561, 84.126, 93.558, 93.563, 93.596, and 93.778
Program Name	Child and Adult Care Food Program Child Nutrition Cluster Supplemental Nutrition Assistance Program Cluster Rehabilitation Services - Vocational Rehabilitation Grants to States Temporary Assistance for Needy Families Cluster Child Support Enforcement Child Care and Development Fund Cluster Medicaid Cluster
Federal Agency	Department of Agriculture Department of Education Department of Health and Human Services
State Agency	Department of Human Services
Federal Award Identification Number	201717N109945, 201717IQ390345, 8044 H126A170063, G1702TNTANF, 1704TNCSES, G1701TNCCDF, 05-1705TN5ADM
Federal Award Year	2017
Finding Type	Significant Deficiency (10.558, 10.559, 10.561, 84.126, 93.563, 93.596, and 93.778) Material Weakness (93.558) Noncompliance
Compliance Requirement	Allowable Costs/Cost Principles
Repeat Finding	N/A
Pass-Through Entity	N/A
Questioned Costs	N/A

Fiscal staff for the Department of Human Services used incomplete, inaccurate information to create cost allocation tables

Background

Because the Department of Human Services administers various public assistance programs, federal regulations require the state to submit a cost allocation plan that outlines the procedures used to identify, measure, and allocate costs to all programs administered by the department. Fiscal staff within the Department of Finance and Administration create and submit the cost allocation plan on behalf of the Department of Human Services, as well as allocate costs to federal grant awards in accordance with the cost allocation plan.

In accordance with federal regulations, fiscal staff allocate administrative costs that cannot be directly charged to a specific federal program to all benefitting federal programs based on the cost allocation plan. During the audit period, July 1, 2016, through June 30, 2017, two cost allocation plans were effective for the department. The first plan was effective July 1, 2016, through March 31, 2017. The second was effective April 1, 2017. A total of $381,213,289 of the department's expenditures during our audit period was subject to allocation under the cost allocation plan. (Federal regulations exclude from cost allocation plans expenditures for financial assistance, medical vendor payments, food stamps, and payments for services and goods provided directly to program recipients.)

According to Title 45, *Code of Federal Regulations*, Part 95, Section 507(a), a cost allocation plan for a state agency must describe the procedures used to identify, measure, and allocate all costs to each of the programs operated by the state agency.

Each quarter, fiscal staff prepare cost allocation tables. Generally, each table covers a specific activity that department staff perform for programs, identifies one or more federal programs to which costs for the activity should be charged, and identifies the percentage of costs associated with the specific activity that should be charged to each federal program.

Fiscal staff then use the cost allocation tables' percentages to prepare cost allocation spreadsheets that identify the amount of expenditures that fiscal staff should allocate to the federal programs administered by the department.

Finally, fiscal staff enter cost allocation entries into the department's accounting system based on the cost allocation calculations documented in the spreadsheets.

Summary of Conditions

Based on testwork performed, we found that the Department Controller did not ensure that fiscal staff adhered to acceptable statistical sampling methods and that fiscal staff allocated costs in accordance with the cost allocation plan and federal requirements. Specifically, we noted that

- the Family Assistance Random Moment Sampling universe did not contain all required staff (see Condition A), and
- fiscal staff did not calculate allocation percentages correctly for costs that benefitted the entire department (see Condition B).

Condition A – The Family Assistance Random Moment Sampling Universe Did Not Contain All Required Staff

Random Moment Sampling

During the audit period, July 1, 2016, through June 30, 2017, fiscal staff for the Department of Human Services allocated approximately $109.9 million in administrative costs to various federal and state funding sources using random moment sampling. According to the *Division of Cost Allocation Best Practices Manual for Reviewing Public Assistance Cost Allocation Plans*, random moment sampling (RMS) is

> . . . a work sampling technique for statistically determining the amount of effort spent by a group of employees on various activities. A RMS study consists of a number of individual observations of employee activities taken at randomly selected points in time. Based on these observations, the total effort of a group of employees can be estimated with a measurable degree of confidence and precision

that the results approximate those had the employees been observed 100% of the time.

According to the *Cost Allocation Plan for the TN Department of Human Services*, RMS is used to identify employee efforts directly related to specific programs and activities and to identify employee effort which is common to more than one program for subsequent distribution of costs to individual programs. Fiscal staff[10] for the Department of Human Services used RMS to allocate costs to four benefitting organizational units during the audit period: Investigations (INV), Adult Protective Services (APS), Field Operations (FO), and Family Assistance (FA).

The State RMS Administrator uploads a list of employees (the sample population universe) into an electronic RMS system. The RMS system randomly selects sample occurrences and employees from the sample population universe. The selected individual uses the RMS system to complete a survey identifying the activities the employee was working on at the sampled moment in time. Per the cost allocation plan, each workday is broken down into one-minute intervals yielding 315 possible strike points per standard workday. The RMS System monitors the number of valid samples received for each survey on a daily basis and adds additional samples during the sample period (each calendar quarter) to meet the required number of valid samples for each organizational unit.

According to Title 2, *Code of Federal Regulations* (CFR), Section 200.430(i)(5)(i) and OMB A-87, Attachment B, Section h(6)(a), the RMS methodology must generally meet acceptable statistical sampling standards including

A. the sampling universe must include all of the employees whose salaries and wages are to be allocated based on sample results . . .;

B. the entire time period involved must be covered by the sample; and

C. the results must be statistically valid and applied to the period being sampled.

During the audit period, of the $109.9 million in administrative costs that fiscal staff allocated using RMS, $85.2 million was based on the RMS results for the Family Assistance division, which is the largest division of the department. Family Assistance staff perform tasks such as eligibility determination for the Supplemental Nutrition Assistance Program, Temporary Assistance for Needy Families, Child Care and Development Fund, and the Medical Assistance Program (Medicaid).

Fiscal staff used the RMS results for January through March 2017 to allocate costs incurred during January through March 2017, as required by federal regulations. In addition, however, fiscal staff used the same January through March 2017 RMS results to allocate costs for the quarter April through June 2017, which is not in accordance with federal requirements (see Finding 2017-010). Because the Family Assistance division is the largest division and the RMS results for January through March 2017 were used to allocate half of the audit period's costs for the division, we tested

[10] On April 11, 2016, the Department of Finance and Administration assumed responsibility for performing the Department of Human Services' fiscal functions, including implementation of the cost allocation plan. Therefore, the Department Controller and other fiscal employees referenced in this finding are employees within the Department of Finance and Administration.

fiscal staff's RMS sampling procedures for the quarter January 1, 2017, through March 31, 2017, to determine whether the RMS universe of employees for the Family Assistance division was complete and accurate.

Audit Procedures for Family Assistance RMS Results

For each of the six, bi-monthly pay periods during January 1, 2017, through March 31, 2017, we reviewed the employees included in the Family Assistance RMS universe, and compared them to the Family Assistance unit's Edison payroll data[11] for January 1, 2017, through March 31, 2017. For the purpose of determining whether the RMS universe was complete, if an employee was excluded from the RMS universe but their payroll records indicated that they were on leave for the entire pay period, we considered the exclusion to be appropriate and did not note any error.

Based on our procedures, we concluded that the Department Controller did not ensure that the Family Assistance RMS methodology followed acceptable statistical methods, because fiscal staff improperly excluded 308 of the 1052 employees who should have been included in the RMS universe (29%) for the quarter ended March 31, 2017. See Table A below for details related to the employees that were excluded from the RMS universe.

Table A
Reasons for Excluding Employees from the Family Assistance RMS Universe for the Quarter Ended March 31, 2017

Descriptions	Number of Employees
New Worker Training	159
Eligibility Assistants	80
Leave, Resigned, or Retired*	48
Not Working in Normal Office location	5
Assigned to Special Family Assistance Projects	4
Multiple**	12
Total Employees	308

*These employees had regular time worked in Edison, the state's accounting system, during the pay period(s) during which they were excluded from the RMS universe.

**These employees had multiple reasons for exclusions during the quarter. For example, for one month, the employee may have been excluded due to New Worker Training, and the next month excluded due to leave.

In addition to these 308 Family Assistance employees, we noted that for the quarter ended June 30, 2017, fiscal staff improperly excluded 260 employees from the RMS universe because they erroneously used the prior periods' RMS results to allocate current quarter costs.

[11] Edison is the State's accounting system. Each pay period, employees have their payroll costs charged to organizational units called department IDs. For this testwork, we reviewed payroll data for department IDs that were designated to have their costs allocated using the Family Assistance RMS system.

In both cases, we noted that these individuals were excluded from the RMS universe because fiscal staff had not established adequate controls for ensuring that exclusions from the RMS universe were appropriate and accounted for properly. Additional details related to the exclusions are provided below.

New Worker Training

For the 159 employees assigned to new worker training, the cost allocation plan did not provide for excluding these employees, and we noted that the RMS process was not designed to ensure that employees were included in the RMS universe as soon as the employees' training was completed. Specifically, the RMS universe is updated every two weeks (every other Friday), so any individual excluded from the universe is excluded for two weeks, even if the employee's new worker training ends the first week of the two-week period. As a result, any time an employee spends working on programmatic activities after new worker training ends and before the end of the two-week sampling period (which occurs every other Friday) is improperly excluded from the RMS universe.

Based on discussion with Family Assistance staff, new worker training is not scheduled to coincide with the two-week RMS sampling periods and could end on any day of the week; therefore, each individual completing new worker training could be improperly excluded from the RMS universe for up to two weeks.

Since excluding these staff was not approved in the plan, and there was no evidence to suggest the employees were in new worker training for the entire sampling periods, we concluded that it was not appropriate to exclude these individuals.

Eligibility Assistants

For the 80 eligibility assistants excluded from the RMS universe, we noted that the job description[12] for these employees and our discussions with fiscal staff suggested that these employees interacted directly with clients, worked directly on applications, and performed eligibility determinations. According to the *Division of Cost Allocation Best Practices Manual for Reviewing Public Assistance Cost Allocation Plans* (Best Practices Manual), Section VI., Part C(4), employees who work directly on cases should normally be included in the universe, or the matter should be explained in the cost allocation plan. In addition, the cost allocation plan did not provide for excluding these employees and stated that all employees performing functions within the organizational unit would be included in the RMS universe.

Per 2 CFR 200.430(i)(5)(ii), the state is permitted to exclude support staff from the RMS universe and instead allocate support staff's costs based on the sampled employees' RMS results. Nevertheless, we included this condition in this finding because "support staff" is not defined in

[12] According to the job description, eligibility assistants' activities include asking applicants questions needed to obtain information related to their eligibility status to determine proper benefit eligibility, documenting information obtained during client interviews into the eligibility determination system, obtaining information from various databases and other needed sources to assist Eligibility Counselors in eligibility determination, and comparing client information to eligibility criteria. The position differs from Eligibility Counselor I in that "Eligibility Counselors perform work of greater scope and complexity to determine needed social services and eligibility for these services."

the regulations and the Best Practices Manual suggests that federal officials may not conclude that individuals working directly on client cases and determining client eligibility are support staff.

Leave, Resigned, or Retired

For the 48 employees that fiscal staff indicated were on leave, had resigned, or had retired, we noted that the payroll records demonstrated that these individuals were working on Family Assistance activities during the applicable sampling period, and they were not actually on leave or out of the office due to resignation or retirement during the entire sampling period. For example, for the pay period January 16, 2017, through January 31, 2017, there were eight individuals excluded from the universe due to being in the "FMLA" (Family and Medical Leave Act) category. Of these eight individuals, we noted that five of them took no leave during the period, and the remaining three took some leave, but they also worked during the period. Since these individuals were working on Family Assistance activities during the period and their costs were allocated based on the Family Assistance RMS results, federal regulations require fiscal staff to include the employees in the RMS universe.

We noted that this matter occurred primarily due to inadequate processes for determining when employees should be excluded due to absences. Specifically, based on discussion with fiscal staff, fiscal staff excluded individuals from the universe due to leave when Human Resources staff indicated that the individuals were *approved* to take extended leave, not necessarily when fiscal staff performed procedures to determine that the employees were not in the office. As a result, we noted many instances in which employees worked for the entire period, but fiscal staff excluded the employees from the RMS universe.

Not Working in Normal Office Location

For five employees, fiscal staff indicated that the employees were working in the community and would not have been able to access the RMS website to complete the survey in time, so fiscal staff excluded the employees. In order for the RMS results to be statistically valid, these individuals were required to be included in the RMS universe, even if they were working remotely. Although fiscal staff's practice was to allocate these individuals' personnel costs based on the RMS results, fiscal staff did not establish a mechanism for obtaining these individuals' survey responses, such as using a mobile device, in the event the employees were randomly selected.

Assigned to Special Family Assistance Projects

For the four employees working on special Family Assistance projects, the employees were working on Family Assistance activities and their costs were allocated using Family Assistance RMS results; therefore, the employees should have been included in the universe. Fiscal staff's documentation indicated that these individuals were excluded because they had no caseloads; however, we noted that the Family Assistance RMS survey had specific options for employees to select if they were working on program activities that were not case specific. In addition, if the special projects were not program specific, the RMS survey also had an option for the employee to indicate that they were working on non-program related tasks. Since these individuals could have used the RMS survey to document their work activities, it is not clear why fiscal staff excluded these individuals.

260 employees were excluded from the RMS universe for the quarter ended June 30, 2017

Beginning April 1, 2017, fiscal staff began allocating all current quarter costs based on the previous quarter's information, which is not in accordance with federal cost principles requirements. This practice resulted in not including all required employees in the Family Assistance RMS universe. Specifically, beginning April 1, 2017, the Field Operations division was blended with the Family Assistance division. Because fiscal staff used the Family Assistance RMS results for the prior quarter, January 1, 2017, through March 31, 2017, to allocate the costs for the quarter April 1, 2017, through June 30, 2017, and the Field Operations staff were excluded from the Family Assistance RMS universe during the prior quarter, none of the 260 Field Operations staff were represented in the RMS universe used to allocate their costs. As a result, for the quarter ended June 30, 2017, fiscal staff allocated approximately $3.4 million in expenditures associated with the Field Operations employees based on invalid statistical data. For more information regarding noncompliance associated with using prior period data to allocate current period costs, see Finding 2017-010.

Condition B – Fiscal Staff Did Not Calculate Allocation Percentages Correctly for Costs that Benefitted the Entire Department

Table 1

Per the cost allocation plan, fiscal staff created Table 1 to allocate costs associated with departmental activities that benefit all programs administered by the department, such as costs associated with the Commissioner's Office. During the audit period, fiscal staff used Table 1 to allocate $43,841,431 in administrative costs to various funding sources.

Table 1 was created using the position count allocation basis. Fiscal staff calculate the average number of filled full and part time positions for each program during a quarter, then use these averages to calculate a percentage for each program based on the proportion of the department's entire workforce for each program. Fiscal staff use staffing assignment data to determine the number of filled full and part time positions for each program.

We tested fiscal staff's Table 1 calculations for the quarter ended March 31, 2017, to determine whether the table was prepared accurately based on employees' working assignments and the cost allocation plan.

Relationship Between Family Assistance RMS Results and Table 1

It is important to note that since Table 1 was created using the staffing assignments of all department employees, and given that employees within the Family Assistance division represent the largest group of employees within the department, the Family Assistance RMS results have a significant impact on Table 1. For example, of the 3,318 department employees included in the data used to create Table 1 for the period January 1, 2017, through March 31, 2017, 1,686 of them (51%) were Family Assistance employees whose personnel costs were allocated via Family Assistance RMS results. Since 51% of the information used to create Table 1 for the quarter was based on Family Assistance RMS information, any inaccuracies in the RMS results could invalidate over half of the Table 1 calculations as well.

Continuing with the example above, if the RMS results showed that 20% of Family Assistance staff's time for the quarter was spent working on Temporary Assistance for Needy Families, for example, fiscal staff would add 337.2 people (1,686 X 20%) to the total number of department employees working on Temporary Assistance for Needy Families during the quarter. In order to ensure costs are allocated via Table 1 based on the proportional benefits that programs receive, these pro-rata calculations should generally occur for all employees whose activities benefit multiple programs.

Due to the significant amount of costs that are allocated through both Table 1 and the Family Assistance Tables, and the relationship between the two, it is critical that fiscal staff maintain adequate controls over the data and processes used to prepare the RMS and Table 1 calculations.

Audit Procedures for Table 1

Based on our review, we determined that the Department Controller did not ensure that fiscal staff prepared Table 1 properly. We noted several deficiencies in the accounting procedures fiscal staff used to calculate Table 1 including the following:

- fiscal staff did not reconcile employees' assignments per the staffing assignment data used to create Table 1 with employees' assignments per payroll data to ensure the table was prepared using accurate information;
- fiscal staff did not prepare Table 1 to properly reflect the effect of temporary staff assignments;
- fiscal staff did not update Table 1 to reflect key changes in the cost allocation methodologies used in the amended cost allocation plan, effective April 1, 2017; and
- fiscal staff improperly excluded employees working in divisions of the department and did not always calculate position counts correctly for included divisions.

Fiscal Staff Did Not Reconcile Key Data Sources

We noted that fiscal staff created Table 1 based on employee roster information, rather than developing the table based on the division to which the employees' payroll costs were charged. According to fiscal staff, reconciliation procedures were not performed to ensure that each employee's payroll costs were charged to the divisions that match their employee roster information. Based on our review of both the roster information and the payroll information for the quarter ended March 31, 2017, we noted that for 70 employees, the programs the employees worked on per the roster information did not agree with the programs the employees worked on per their payroll information. This is a critical control deficiency, as differences between the payroll data and the employee roster information mean that either Table 1 was created incorrectly based on erroneous employee roster information or that employee payroll costs were charged incorrectly to federal programs because employees were working in one division but their payroll costs were charged to another division, or both. We were unable to determine which of these scenarios applied to these individuals. See Finding 2017-015, Condition A, Testwork for payroll costs charged to the incorrect department ID, for more information.

Fiscal staff did not prepare Table 1 to properly reflect the effect of employees placed on temporary work assignments

For the quarter January 1, 2017, through March 31, 2017, fiscal staff's records indicated that there were 107 employees working on temporary assignments. The time that employees spend working on temporary assignments is generally tracked using timesheets. When preparing table 1, fiscal staff assumed that the employees spent 100% of their time working in their normal staff assignments instead of determining the actual time spent working on the temporary assignments so that fiscal staff could include an accurate number of employees in the position count calculation for the temporary assignment.

Fiscal staff did not update Table 1 to reflect key changes

We also noted that the fiscal staff did not update Table 1 to reflect key changes in the cost allocation methodologies used in the amended cost allocation plan, effective April 1, 2017, for 54 employees. When calculating the total number of filled positions for the Child Support Enforcement program (CSE), for example, fiscal staff included six employees working in the Information Technology division on Child Support activities, even though the Information Technology employees' payroll costs were already allocated to all federal programs via Table 1.[13] This accounting treatment is not consistent with federal cost principles.[14]

Fiscal staff improperly excluded employees working in divisions of the department and did not always calculate position counts correctly for included divisions

As discussed in the Background section, when calculating the number of Family Assistance staff to include in Table 1 for each program, fiscal staff multiply the total Family Assistance staff count by each federal program's RMS results percentage to calculate each program's pro rata share of Family Assistance staff positions. We noted, however, that fiscal staff did not perform these pro rata calculations for 63 staff working in the Investigations Division and 14 staff working in the Office of General Counsel Field Staff Division; therefore, these 77 staff were excluded from the Table 1 calculations. In other cases, staff working on multiple programs were included in Table 1, but fiscal staff included the employees in the incorrect program count or calculated the pro rata share using the incorrect cost allocation table.

Recalculation of Table 1

For April 1, 2017, through June 30, 2017, to obtain an understanding of the potential impact these errors had on the quarter, we recalculated Table 1 based on the updated methodologies in the amended cost allocation plan, and included the appropriate department employees in our calculations. We calculated the pro rata share of position counts for all of the employees using the

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[13] The costs were allocated to all programs because the amended cost allocation plan provided for temporarily allocating costs for four divisions using Table 1 until fiscal staff could determine a more appropriate allocation method.

[14] If fiscal staff have evidence that the employee's activities for the quarter benefitted only one federal program, such as CSE (and thus fiscal staff should include the employee in the CSE position count), federal regulations would prohibit allocating the payroll costs as indirect costs to all programs for that quarter. Conversely, if fiscal staff determined that the employee's activities benefitted all programs (and thus fiscal staff allocated the costs to all programs via Table 1), including the employee in the CSE position count would be inappropriate, as the employee's activities did not benefit only CSE.

applicable cost allocation methodology. In order to obtain an understanding of the difference between preparing the table based on staffing data, which was fiscal staff's practice, and preparing it based on payroll data, we based our calculations on payroll data and assumed the employees worked in the same division to which their payroll costs were charged.

After preparing our version of Table 1 for the quarter, we allocated the quarter's costs to programs using our table and compared our allocation amounts to the amounts fiscal staff allocated for the quarter. See Table B below for the differences in the allocated amounts for each program and Table C below for the differences in the position counts calculated for each program.

Table B

Potential Overcharges (Undercharges) By Program Due to Calculating Table 1 Incorrectly for the Period April 1, 2017, through June 30, 2017

Program	Federal Expenditures	State Expenditures	Total Expenditures
Programs Overcharged			
Child Care and Development Block Grant	$ -	$13,175	$13,175
Child Support Enforcement	36,110	18,602	54,712
Community Services Block Grant	85	-	85
Medical Assistance Program	12,725	12,725	25,450
Social Security Disability Insurance	29,958	-	29,958
Vocational Rehabilitation	107,860	31,022	138,882
Total	**$186,738**	**$75,524**	**$262,262**
Programs Undercharged			
Independent Living Services for Older Individuals Who Are Blind	$(38,717)	$(4,302)	$(43,019)
State Administrative Expenses for Child Nutrition	(6,677)	-	(6,677)
Supplemental Nutrition Assistance Program	(59,563)	(59,563)	(119,126)
Social Services Block Grant	(70,900)	-	(70,900)
Temporary Assistance for Needy Families	(11,270)	(11,270)	(22,540)
Total	**$(187,127)**	**$(75,135)**	**$(262,262)**

Table C

Differences in Table 1 Employee Counts by Activity for the Period April 1, 2017, through June 30, 2017

Activity	Difference
Employees Overcounted	
Appeals and Hearings	1
Child Support Enforcement	6
Medical Assistance Program	3
Vocational Rehabilitation	15
Total	**25***
Employees Undercounted	
Adult Protective Services	(2)
Assistive Technology	(1)
Child Care and Development Block Grant	(1)
Independent Living Services for Older Individuals Who Are Blind	(6)
Social Services Block Grant	(9)
State Administrative Expenses for Child Nutrition	(1)
Supplemental Nutrition Assistance Program	(35)
Temporary Assistance for Needy Families	(6)
Total	**(61)***

*Note: The amounts of over- and undercounted areas do not net to zero due to fiscal staff not including as many employees in their calculations as we did in ours.

As noted previously, fiscal staff use Family Assistance RMS data to prepare Table 1; therefore, any errors included in the RMS results (such as the matters discussed in Condition A above) are reflected in Table 1 as well.

Given the nature and scope of the errors related to the Family Assistance RMS and Table 1 calculations, and the fact that we did not always have sufficient information to perform accurate recalculations (such as accurate data identifying employees' activities), we did not attempt to calculate questioned costs related to the noncompliance noted in this finding.

Condition C – Risk Assessment

Given the problems identified during our fieldwork, we also reviewed the Department of Human Services' November 2016 Financial Integrity Act Risk Assessment and determined that top management assessed the risk that "Costs charged to a federal program are not allowable under program regulations" as having a remote likelihood and small impact; however, management did not identify any mitigating controls related to the issue. Given the unallowable costs and cost principles issues identified in this finding and others during the current audit, such as 2017-015, 2017-033, and 2017-037, we concluded that management should have assessed the likelihood as reasonably possible, assessed the impact as large, and included a control activity to mitigate the risk in the department's annual risk assessment.

Criteria

Title 2, *Code of Federal Regulations* (CFR), Part 200, Section 430(i)(5)(i) and OMB Circular A-87, "Cost Principles for State, Local and Indian Tribal Governments," Attachment B, Section 8(h)(6)(a), state that substitute systems which use sampling methods must meet acceptable statistical sampling standards including:

> (A) The sampling universe must include all of the employees whose salaries and wages are to be allocated based on sample results . . . [except that less than full compliance with the statistical sampling standards may be accepted by the cognizant agency if the cognizant agency makes certain determinations];
>
> (B) The entire time period involved must be covered by the sample; and
>
> (C) The results must be statistically valid and applied to the period being sampled.

According to the department's cost allocation plan, "The universe for the [RMS] surveys will be comprised of all employees performing functions within each organizational unit."

Per 45 CFR 95.517(a), "A State must claim FFP [federal financial participation] for costs associated with a program only in accordance with its approved cost allocation plan." This requirement is effectively extended to all programs administered by state public assistance agencies by Section C, Appendix VI, of Title 2, CFR, Part 200 (formerly Section C of OMB A-87, Attachment D), which states,

> State public assistance agencies will develop, document and implement, and the Federal Government will review, negotiate, and approve, public assistance cost allocation plans in accordance with Subpart E of 45 CFR Part 95. The plan will include all programs administered by the state public assistance agency.

The *Division of Cost Allocation Best Practices Manual for Reviewing Public Assistance Cost Allocation Plans,* Section VI., Part C(4), states:

> The sample universe should normally include all workers with direct client contact (direct workers). The PA plan should clearly identify and explain why any direct workers are excluded from the sample universe.

Cause

Based on discussion with fiscal staff, fiscal staff excluded individuals from the RMS universe that were potentially on leave, resigned, or retired because fiscal staff believed that including these individuals would invalidate the results of the sample. We did not identify any evidence that supported that including these individuals in the RMS universe would result in invalidating the statistical results, and the federal regulations required the individuals to be included.

Regarding improper calculations for Table 1, based on discussion with fiscal staff, fiscal staff was not aware that employee assignments per payroll data did not agree with employee assignments per roster information. In addition, for the Table 1 calculations for the quarter ended June 30, 2017, fiscal staff did not appear to consider the impact that a revision in the cost allocation plan would have on the cost allocation tables prepared for the prior quarter.

Effect

Failure to allocate costs in accordance with the cost allocation plan and federal requirements increases the risk that fiscal staff will fail to assign an appropriate share of costs to programs and that federal grantors will disallow costs charged to federal programs.

Additionally, federal regulations address actions that federal agencies may impose in cases of noncompliance. As noted in 2 CFR 200.338, "If a non-Federal entity fails to comply with Federal statutes, regulations or the terms and conditions of a Federal award, the Federal awarding agency or pass-through entity may impose additional conditions," including, as described in Section 200.207, "Specific conditions":

(1) Requiring payments as reimbursements rather than advance payments;

(2) Withholding authority to proceed to the next phase until receipt of evidence of acceptable performance within a given period of performance;

(3) Requiring additional, more detailed financial reports;

(4) Requiring additional project monitoring;

(5) Requiring the non-Federal entity to obtain technical or management assistance; or

(6) Establishing additional prior approvals.

Furthermore, Section 200.338 also states,

> If the Federal awarding agency or pass-through entity determines that noncompliance cannot be remedied by imposing additional conditions [as described above], the Federal awarding agency or pass-through entity may take one or more of the following actions, as appropriate in the circumstances:
>
> (a) Temporarily withhold cash payments pending correction of the deficiency by the non-Federal entity or more severe enforcement action by the Federal awarding agency or pass-through entity.
>
> (b) Disallow (that is, deny both use of funds and any applicable matching credit for) all or part of the cost of the activity or action not in compliance.
>
> (c) Wholly or partly suspend or terminate the Federal award.
>
> (d) Initiate suspension or debarment proceedings as authorized under 2 CFR part 180 and Federal awarding agency regulations (or in the case of a pass-through entity, recommend such a proceeding be initiated by a Federal awarding agency).

(e) Withhold further Federal awards for the project or program.

(f) Take other remedies that may be legally available.

Recommendation

The Department Controller should ensure that the Department of Human Services' Random Moment Sampling universe includes all applicable moments for all direct worker employees in the universe whose salaries and wages are to be allocated based on the sample results. In addition, the Department Controller should establish processes to ensure that Table 1 calculations are accurate and that the calculations

- properly reflect the effect of temporary assignments;
- are updated to reflect changes in cost allocation methodologies, as needed;
- include all employees working in the department (except those whose personnel costs are allocated via Table 1); and
- include all necessary pro-rata calculations.

Finally, the Department Controller should ensure that fiscal staff and management establish adequate internal controls to resolve all errors noted above, including a comprehensive reconciliation process for payroll data and staffing assignment data.

The Commissioner of the Department of Human Services should assess all significant risks with sufficient attention to the impact and likelihood of the risk. The risk assessment and the mitigating controls should be adequately documented and approved by the Commissioner, who should implement effective controls to ensure compliance with applicable requirements, assign employees to be responsible for ongoing monitoring of the risks and any mitigating controls, and take action if deficiencies occur.

Management's Comment

We concur in part.

Condition A. The Family Assistance Random Moment Sampling Universe Did Not Contain All Required Staff

We do not concur.

Management is concerned that the interpretation of the regulations throughout this condition may be more rigid than intended, and that the cost of implementing a corrective action plan that satisfies this rigid interpretation will far exceed the benefits to be achieved by such a plan. The underlying premise behind the entire sampling process is that costs are difficult to assign to any one benefitting program; therefore, another means of assigning cost was developed. The auditor's interpretation of the regulations as it pertains to inclusion in the sampling universe is so precise that it mirrors procedures that would be performed were the employees completing timesheets that charged costs directly to the benefiting federal program. The finding cites Title 2, *Code of Federal Regulations* (CFR), Section 200.430. This section of the guidance also includes additional information on standards for personnel charges which state that charges to federal awards for salaries must be supported by a system of internal control which provides reasonable assurance that the charges are accurate, allowable, and properly allocated (emphasis provided). The charges must also comply with established accounting policies and practices of the department. To that end, we believe our current process for RMS inclusion or exclusion is reasonable and is consistent with the Federal established practices of the department. Additionally, the same section of the Federal guidance states, "Less than full compliance with the statistical sampling standards noted in subsection (5)(i) may be accepted by the cognizant agency for indirect costs if it concludes that the amounts to be allocated to Federal awards will be minimal, or if it concludes that the system proposed by the non-Federal entity will result in lower costs to Federal awards than a system which complies with the standards." Management maintains that the methodologies being utilized by management result in a lower cost to the federal awards than processes that would need to be put in place to address the identified concerns.

In regard to the specific items noted in the findings,

New Worker Training

As indicated in the finding, the RMS universe was updated every two weeks during the audit period. Management believes that a twice a month control is reasonable given the nature of the costs being incurred and the additional costs associated with the auditor's suggestion of revising this to a daily control. It is also reasonable to assume that an employee who just completed training (even if it was in week 1 of a 2 week period) would rely on a seasoned employee to continue providing guidance; thus, the new employee's costs would mirror the time charged by the employee that was already included in the RMS universe.

Eligibility Assistants

Eligibility assistants are excluded from the RMS universe in accordance with 2 CFR 200.430(i)(5)(ii). The department is permitted to exclude support staff. As indicated in footnote 12, Eligibility assistants "... assist Eligibility Counselors in eligibility determination..." The assistants are not authorized to make eligibility determinations for the program.

Other Categories

The aggregate total of employees noted for the other categories approximates 2% of the RMS universe. Management does not consider their exclusion to have a material effect on the completeness of the universe; however, management will explore cost effective means to include them if possible.

260 employees excluded from the RMS Universe for the quarter ended June 30, 2017

The auditors were provided evidence documenting the fact that the methodology is in accordance with an approved Public Assistance Cost Allocation Plan, and that a clear intention to make appropriate quarter adjustments after subsequent analysis is completed had been discussed with and understood and accepted by federal partners. Please reference management's response to finding 2017-010.

Condition B. Fiscal Staff Did Not Calculate Allocation Percentages Correctly for Costs that Benefitted the Entire Department

We concur in part.

Fiscal staff did not reconcile key data sources

Staffing pattern data and payroll queries were not reconciled. Employees were counted based on how they appeared on the system generated staffing pattern. A reconciliation process will be developed by June 30, 2018.

Fiscal staff did not prepare Table 1 to properly reflect the effect of employees placed on temporary work assignments.

The primary program assignment was used to determine the count for people working on temporary assignments and was not split proportionally between the timesheet data relating to time spent on the temporary assignment and their primary assignment. 2 CFR 200 indicates that short term fluctuations between workload categories need not be considered as long as the distribution of salaries and wages is reasonable over the longer term. While this specific reference is for budget estimates, it appears to support the federal government's acceptance of an approach that, while not exact, is operationally efficient as long as the result is reasonable.

Remaining conditions

The 6 employees mentioned in the audit findings were counted as dedicated child support employees in Table 1 based on the prior quarter statistics that were used to allocate current quarter costs according to the approved April 1, 2017 cost allocation plan. Counts related to the investigations unit and the offices of general counsel were improperly excluded from Table 1. They will be included going forward based on the proportional benefit to programs based on the tables developed and their related statistics.

Condition C. Risk Assessment

The department completes its annual risk assessment as required under *Tennessee Code Annotated*, Section 9-18-101 using guidance provided by the Tennessee Department of Finance and Administration (F&A). The Department's November 2016 Financial Integrity Act Risk Assessment risks of non-compliance were assessed by compliance type requirement for the Department as a whole. For the December 2017 Financial Integrity Act Risk Assessment, based on revised F&A guidance, risks were assessed on a more programmatic/divisional level.

Auditor's Comment

Condition A – The Family Assistance Random Moment Sampling Universe Did Not Contain All Required Staff

Management did not address the insufficiency of their sampling universe, which is the basis for Condition A. Management's concerns involve the costs of addressing this condition; however, most of the issues in Condition A are the result of fiscal staff performing work that we believe is not necessary and actually leads to noncompliance with RMS requirements. Specifically, the department's RMS system automatically selects additional individuals for sampling if an individual does not respond timely; therefore, there is no need for fiscal staff to spend time maintaining deactivated listings and removing employees from the universe due to leave, new worker training, and similar issues.

We contacted management, explained why we believed compliance would actually be less costly, and asked why management believes the changes would be costly; however, management would not provide an explanation and simply stated, "Yes, we believe that our response reflects the way we think about that."

New Worker Training

Regarding management's biweekly process for updating the RMS universe, management refers to "the auditor's suggestion of revising this to a daily control." We are not suggesting that the department perform this process daily and have made no recommendation related to the frequency of the RMS universe update. On the contrary, we believe the department should simply use its RMS system as designed and not exclude these employees from the RMS universe.

Other Categories

Regarding management's determination that "The aggregate total of employees noted for the other categories approximates 2% of the RMS universe," management appears to have omitted the Leave, Resigned, or Retired category from management's calculations. After adding this category, the aggregate total of employees for the categories other than New Worker Training and Eligibility Assistants is roughly 6.6% of the RMS universe.

Finding Number	2017-012
CFDA Number	10.559, 10.560, 10.561, 84.126, 84.177, 93.558, 93.563, 93.569, 93.667, 93.778, and 96.001
Program Name	Child Nutrition Cluster State Administrative Expenses for Child Nutrition Supplemental Nutrition Assistance Program Cluster Rehabilitation Services - Vocational Rehabilitation Grants to States Rehabilitation Services - Independent Living Services for Older Individuals Who are Blind Temporary Assistance for Needy Families Cluster Child Support Enforcement Community Services Block Grant Social Services Block Grant Medicaid Cluster Disability Insurance/Supplemental Security Income Cluster
Federal Agency	Department of Agriculture Department of Education Department of Health and Human Services Social Security Administration
State Agency	Department of Human Services
Federal Award Identification Number	201717N109945, 201616N253345, 201717N253345, 201616IS251445, 201717IS251445, 8044 H126A160063, 8044 H126A170063, H177B160064, H177B170064, G1502TNTANF, G1602TNTANF, 1604TNCSES, 1704TNCSES, G16B1TNCOSR, G1501TNSOSR, G1601TNSOSR, 05-1605TN5ADM, 05-1705TN5ADM, 8826 04-16-04TNDI00, and 8826 04-17-04TNDI00
Federal Award Year	2015 through 2017
Finding Type	Significant Deficiency (10.559, 10.561, 84.126, 93.558, 93.563, and 93.778) Noncompliance
Compliance Requirement	Allowable Costs/Cost Principles
Repeat Finding	N/A
Pass-Through Entity	N/A

Questioned Costs

CFDA	Federal Award Identification Number	Amount
10.559	201717N109945	$27
10.560	201616N253345	$1
10.560	201717N253345	$2,262
10.561	201616IS251445	$1
10.561	201717IS251445	$183,668
84.126	8044 H126A160063	$1
84.126	8044 H126A170063	$72,854
84.177	H177B160064	$1
84.177	H177B170064	$5,603
93.558	G1502TNTANF	$31,480

93.558	G1602TNTANF	$1
93.563	1604TNCSES	$1
93.563	1704TNCSES	$17,247
93.569	G16B1TNCOSR	$251
93.667	G1501TNSOSR	$1
93.667	G1601TNSOSR	$28,878
93.778	05-1605TN5ADM	$1
93.778	05-1705TN5ADM	$6,004
96.001	8826 04-16-04TNDI00	$1
96.001	8826 04-17-04TNDI00	$87,165

Fiscal staff within the Department of Human Services charged unallowable costs to federal programs during the cost allocation process, including charging costs disallowed by a federal grantor back to federal grant awards, resulting in known federal and state questioned costs of $435,448, and $308,152, respectively

Background

Because the Department of Human Services administers various public assistance programs, federal regulations require the state to submit a cost allocation plan that outlines the procedures used to identify, measure, and allocate costs to all programs administered by the department. Fiscal staff within the Department of Finance and Administration create and submit the cost allocation plan on behalf of the Department of Human Services, as well as allocate costs to federal grant awards in accordance with the cost allocation plan.

In accordance with federal regulations, fiscal staff allocate administrative costs that cannot be directly charged to a specific federal program to all benefitting federal programs based on the cost allocation plan. During the audit period, July 1, 2016, through June 30, 2017, two cost allocation plans were effective for the department. The first plan was effective July 1, 2016, through March 31, 2017. The second was effective April 1, 2017. A total of $381,213,289 of the department's expenditures during our audit period was subject to allocation under the cost allocation plan. (Federal regulations exclude from cost allocation plans expenditures for financial assistance, medical vendor payments, food stamps, and payments for services and goods provided directly to program recipients.)

According to Title 45, *Code of Federal Regulations*, Part 95, Section 507(a), a cost allocation plan for a state agency must describe the procedures used to identify, measure, and allocate all costs to each of the programs operated by the state agency.

Each quarter, fiscal staff prepare cost allocation tables. Generally, each table covers a specific activity that department staff perform for programs, identifies one or more federal programs to which costs for the activity should be charged, and identifies the percentage of costs associated with the specific activity that should be charged to each federal program.

Fiscal staff then use the cost allocation tables' percentages to prepare cost allocation spreadsheets that identify the amount of expenditures that fiscal staff should allocate to the federal programs administered by the department.

Finally, fiscal staff enter cost allocation entries into the department's accounting system based on the cost allocation calculations documented in the spreadsheets.

Cost Pools

Fiscal staff[15] allocate expenditures included in cost pools to various federal programs. A cost pool is essentially a group of expenditures that fiscal staff allocate to various state and federal programs using a specific allocation methodology during the cost allocation process. To ensure that no unallowable costs are allocated to federal programs during the cost allocation process, all unallowable costs must be removed from cost pools prior to allocating the costs to federal awards.

Audit Procedures

To determine whether expenditures included in cost pools were allowable, we performed a cursory review of expenditures that were included in cost pools and subsequently allocated to federal programs for the audit period, July 1, 2016, through June 30, 2017, and tested unusual transactions we identified. We then selected a sample of 32 expenditure transactions from the cost pools identified in fiscal staff's cost allocation schedules for the audit period, July 1, 2016, through June 30, 2017. Because fiscal staff allocated expenditures in three separate groups—salaries and wages, benefits, and all other expenditure categories (non-payroll expenditures)—we stratified our sample based on these three groups, which resulted in testing 13 non-payroll expenditures. The table below identifies the dollar amount of the non-payroll expenditures in the population by program after the costs were allocated to various federal programs.

Table 1
Non-payroll Expenditures Charged to Cost Pools and Allocated to Federal Programs

Program	Total Expenditures
Child and Adult Care Food Program (CACFP)	$297,575
Summer Food Service Program for Children (SFSP)	$200,056
State Administrative Expenses for Child Nutrition (SAE)	$548,786
Supplemental Nutrition Assistance Program (SNAP)	$45,834,926
Supplemental Nutrition Assistance Program (SNAP) Recipient Trafficking Prevention Grants	$532,434
Rehabilitation Services – Vocational Rehabilitation Grants to States (VR)	$5,083,089
Independent Living Services for Older Individuals Who are Blind Program (ILOB)	$264,272
Temporary Assistance for Needy Families (TANF)	$26,770,025
Child Support Enforcement (CSE)	$2,784,664
Community Services Block Grant (CSBG)	$131,554

[15] On April 11, 2016, the Department of Finance and Administration assumed responsibility for performing the Department of Human Services' fiscal functions, including implementation of the cost allocation plan. Therefore, the Department Controller and other fiscal employees referenced in this finding are employees within the Department of Finance and Administration.

Child Care and Development Fund (CCDF)	$5,340,451
Social Services Block Grant (SSBG)	$2,347,727
Medical Assistance Program (MAP)	$5,106,325
Social Security Disability Insurance (SSDI)	$3,727,881
State Expenditures	$1,712,438
Grand Total	**$100,682,203**

Source: Summarized using cost allocation documentation from fiscal staff.

Based on our testwork, we found that fiscal staff allocated unallowable costs to federal programs, including costs that had already been disallowed by the federal government (Condition A) and unallowable meeting costs (Condition B), and we found that a subrecipient overcharged a federal program for depreciation expense (Condition C) resulting in total known questioned costs of $743,600.

<u>**Condition A.** Allocation of Disallowed Costs to Federal Programs</u>

Based on our review of unusual expenditures included in cost pools, we noted that fiscal staff improperly included $743,572 of previously disallowed Vocational Rehabilitation Grants to States costs in their cost allocation calculations for the period October 2016 through December 2016. The VR costs were disallowed because the Assistant Secretary for Special Education and Rehabilitative Services within the U.S. Department of Education had found that Tennessee spent VR funds in violation of VR program requirements and for goods and services that could not be allocated to the VR program. The $743,572 represented a settlement payment for the disallowed costs.

Including these costs in the calculations resulted in fiscal staff reallocating the disallowed costs to most of the programs administered by the department, including back to the Vocational Rehabilitation program. We questioned all disallowed costs that the department reallocated to a federal program. After we brought this matter to the attention of fiscal staff, we verified that fiscal staff created an adjustment entry to reverse these disallowed costs during field work on December 14, 2017, after our audit scope. See Table 2 below for more information.

Table 2
Disallowed Costs Reallocated to Federal Programs

Program	Federal Expenditures	State Matching Expenditures	Total Expenditures
Child Care and Development Block Grant	$0	$57,828	$57,828
Community Services Block Grant	$251	$0	$251
Child Support Enforcement	$17,247	$8,885	$26,132
Independent Living Services for Older Individuals Who Are Blind	$5,603	$623	$6,226
Medical Assistance Program	$6,004	$6,004	$12,008
State Administrative Expenses for Child Nutrition	$2,262	$0	$2,262

Program	Federal Expenditures	State Matching Expenditures	Total Expenditures
Summer Food Service Program	$14	$0	$14
Supplemental Nutrition Assistance Program	$183,668	$183,668	$367,336
Social Services Block Grant	$28,878	$0	$28,878
Social Security Disability Insurance	$87,165	$0	$87,165
Temporary Assistance for Needy Families	$31,480	$31,480	$62,960
Vocational Rehabilitation	$72,854	$19,658	$92,512
Totals	**$435,426**	**$308,146**	**$743,572**

Source: Summarized using accounting records from Edison, the state's accounting system, and cost allocation documentation from fiscal staff.

Condition B. Allocation of Unallowable Meeting Costs to Federal Programs

Based on our sample testwork, fiscal staff allocated unallowable costs to various federal programs for 1 of 13 non-payroll expenditures tested (8%). Based on review of the supporting documentation for the transaction, the expenditure was a portion of a payment to reimburse an employee for meeting supplies, including decorations, candy, gum, and beverages. The description of the reimbursement request was "Materials – TDA [Tennessee DHS Accountability Process] Blow-Out," and per discussion with department staff, these meetings occurred biweekly during the audit period, but are no longer occurring. We concluded that the expenditures were unallowable, because the costs did not appear to be necessary and reasonable for the administration of federal awards, as required by federal regulations.

Condition C. Unallowable Depreciation Expense

In our *Single Audit Report* for 2016, we published a repeat finding (Finding 2016-068) because a subrecipient improperly used federal funds received from various state agencies to pay for the acquisition of its central office building. Although federal regulations prohibit the use of federal funds to acquire real property, these regulations permit non-federal entities to use federal funds to pay for building depreciation. The subrecipient used federal funds from the Summer Food Service Program received through the department to pay for building depreciation that was not calculated in accordance with Generally Accepted Accounting Principles (GAAP). Building depreciation in accordance with GAAP is calculated based on the cost of the building. Based on our review of the subrecipient's valuation of depreciation expense for the central office building, an appraised value in excess of the cost of the building was used to calculate deprecation.

Condition D. Risk Assessment

Given the problems identified during our fieldwork, we also reviewed the Department of Human Services' November 2016 Financial Integrity Act Risk Assessment and determined that top management assessed the risk that "Costs charged to a federal program are not allowable under program regulations" as having a remote likelihood and small impact. Given the unallowable costs identified in this finding and others during the current audit, such as 2017-015, 2017-033, and 2017-037, we concluded that management should have assessed the likelihood as reasonably possible, assessed the impact as large, and included a control activity to mitigate the risk in the department's annual risk assessment.

Criteria

Regarding unallowable costs, 2 CFR 200.441 states,

> Costs resulting from non-Federal entity violations of, alleged violations of, or failure to comply with, Federal, state, tribal, local or foreign laws and regulations are unallowable, except when incurred as a result of compliance with specific provisions of the Federal award, or with prior written approval of the Federal awarding agency.

In addition, 2 CFR 200.403 states,

> Except where otherwise authorized by statute, costs must meet the following general criteria in order to be allowable under Federal awards:
>
> (a) Be necessary and reasonable for the performance of the Federal award and be allocable thereto under these principles.

Finally, 2 CFR 200.436(c) states,

> Depreciation is computed applying the following rules. The computation of depreciation must be based on the **acquisition cost** [emphasis added] of the assets involved . . .

Cause

Regarding the disallowed Vocational Rehabilitation costs allocated to various programs, we noted that costs charged to the disallowed cost accounting code appeared to be rare, and fiscal staff did not appear to have a process in place to consistently filter out the disallowed code. Regarding the employee reimbursement for unallowable meeting costs, we noted that fiscal staff did not appear to have established a method for classifying unallowable costs for employee reimbursements so they could be quickly identified and excluded from cost allocation pools during the cost allocation process. The Fiscal Director for the subrecipient stated that he had used the "Appraisal Cost" approach to calculating depreciation; he was not aware that this was not in conformity with GAAP.

Effect

Charging unallowable costs to federal programs increases the risk that the federal government will disallow the costs and seek recovery of the funds. Additionally, federal regulations address actions that may be imposed by federal agencies in cases of noncompliance. As noted in 2 CFR 200.338, "If a non-Federal entity fails to comply with Federal statutes, regulations or the terms and conditions of a Federal award, the Federal awarding agency or pass-through entity may impose additional conditions," including, as described in Section 200.207, "Specific conditions":

> (1) Requiring payments as reimbursements rather than advance payments;

(2) Withholding authority to proceed to the next phase until receipt of evidence of acceptable performance within a given period of performance;

(3) Requiring additional, more detailed financial reports;

(4) Requiring additional project monitoring;

(5) Requiring the non-Federal entity to obtain technical or management assistance; or

(6) Establishing additional prior approvals.

Furthermore, 2 CFR 200.338 also states,

> If the Federal awarding agency or pass-through entity determines that noncompliance cannot be remedied by imposing additional conditions [as described above], the Federal awarding agency or pass-through entity may take one or more of the following actions, as appropriate in the circumstances:
>
> (a) Temporarily withhold cash payments pending correction of the deficiency by the non-Federal entity or more severe enforcement action by the Federal awarding agency or pass-through entity.
>
> (b) Disallow (that is, deny both use of funds and any applicable matching credit for) all or part of the cost of the activity or action not in compliance.
>
> (c) Wholly or partly suspend or terminate the Federal award.
>
> (d) Initiate suspension or debarment proceedings as authorized under 2 CFR part 180 and Federal awarding agency regulations (or in the case of a pass-through entity, recommend such a proceeding be initiated by a Federal awarding agency).
>
> (e) Withhold further Federal awards for the project or program.
>
> (f) Take other remedies that may be legally available.

Questioned Costs and Other Required Reporting

Questioned Costs

We questioned $435,448 in federal expenditures charged to federal awards, as well as $308,152 in state matching expenditures, for a total of $743,600 in questioned costs. See Tables 2 and 3 above for more details.

This finding, in conjunction with findings 2017-010 and 2017-013 (which also included federal questioned costs for the federal compliance requirement Allowable Costs/Cost Principles), results in total known federal questioned costs exceeding $25,000 for a type of compliance requirement for a federal program.

Concerning questioned costs, 2 CFR 200.516(a)(3) requires us to report known questioned costs that are greater than $25,000 for a type of compliance requirement for a major program.

Additionally, 2 CFR 200.516(a)(4) requires us to report known questioned costs that are greater than $25,000 for a federal program which is not audited as a major program.

According to 2 CFR 200.84,

> *Questioned cost* means a cost that is questioned by the auditor because of an audit finding:
>
> (a) Which resulted from a violation or possible violation of a statute, regulation, or the terms and conditions of a Federal award, including for funds used to match Federal funds;
>
> (b) Where the costs, at the time of the audit, are not supported by adequate documentation; or
>
> (c) Where the costs incurred appear unreasonable and do not reflect the actions a prudent person would take in the circumstances.

Other Required Reporting

In order to fulfill our reporting responsibilities under 2 CFR 200.516, we are also required to include the following information in this finding. See Table 3 for a summary of the errors identified in Condition B above.

Table 3
Summary of Sample Testwork Errors

Program	Population Total	Dollar Amount of Sample Items Tested	Federal Questioned Costs in Sample	State Questioned Costs in Sample	Total Dollar Amount of Error in Sample
SFSP	$200,056	$1	$0	$0	$0
SAE	$548,786	3	1	0	1
SNAP	$45,834,926	511	1	1	2
VR	$5,083,089	117	1	1	2
ILOB	$264,272	7	1	0	1
TANF	$26,770,025	86	1	1	2
CSE	$2,784,664	41	1	1	2
CSBG	$131,554	1	0	0	0
CCDF	$5,340,451	72	0	1	1
SSBG	$2,347,727	225	1	0	1
MAP	$5,106,325	138	1	1	2
SSDI	$3,727,881	104	1	0	1
Grand Total	**$98,139,756**	**$1,306**	**$9**	**$6**	**$15**

Regarding Condition C above, we questioned $13 in federal costs charged to the Summer Food Service Program due to unallowable depreciation expense.

Even though the errors noted for Conditions B and C are small dollar errors, when Condition B's errors are projected to the population and both conditions are combined with known questioned costs described in other findings (see Questioned Cost sections), the questioned costs for the errors far exceed $25,000 for each federal program identified in Conditions B and C. Title 2, *Code of Federal Regulations* (CFR), Section 200.516(a)(3), requires us to report known questioned costs when likely questioned costs are greater than $25,000 for a type of compliance requirement for a major program.

Recommendation

The Department Controller should ensure that employees are trained regarding unallowable costs and perform procedures to identify unallowable costs during the cost allocation process. The Department Controller should also establish a mechanism for classifying or otherwise tracking unallowable employee reimbursements in accounting records so that the unallowable costs can be quickly identified and excluded from cost allocation pools. The Commissioner of the Department of Human Services should take the necessary steps to ensure that subrecipients are aware of the allowable uses of grant funds and that subrecipients' expenditures are properly reviewed.

The Commissioner should assess all significant risks with suffieient attention to the impact and likelihood of the risk. The risk assessment and the mitigating controls should be adequately documented and approved by the Commissioner, who should implement effective controls to ensure compliance with applicable requirements, assign employees to be responsible for ongoing monitoring of the risks and any mitigating controls, and take action if deficiencies occur.

Management's Comment

Condition A

We concur that disallowed costs related to the Vocational Rehabilitation Program were improperly included in expenditures that were cost allocated to multiple federal programs. The department corrected this issue by reversing the impact the improper allocation had on the federal programs. In December 2017, management implemented controls over the cost allocation process to ensure disallowed costs are excluded from the cost allocation process based on the general ledger account associated with this type of transaction.

Condition B

We concur that unallowable meeting costs were charged to federal programs. The department will prepare and post a correcting journal entry to correct funding related to these expenditures by March 31, 2018. While individual travel claims are initially approved by the employee's direct supervisor, fiscal will evaluate its current role in the process and strengthen related controls by June 30, 2018.

Condition C

We do not concur.

The subrecipient noted in condition C does not owe the department any federal funds regarding the building as of June 28, 2017. The department recouped all unallowed costs that were determined questionable in acquiring the building, in the amount of $56,824.50. In fact, the department provided the state auditors and state audit management with a copy of the check and supporting documents to demonstrate that the subrecipient repaid the unallowed amounts to resolve the prior Single Audit finding.

The state auditors stated that "Regarding Condition C above, we questioned $13 in federal costs charged to the Summer Food Service Program due to unallowable depreciation expense." While depreciation is an accounting transaction to reduce a property cost, there is no actual cash for depreciation paid to the subrecipient for the state auditors to question as of June 28, 2017.

Condition D. Risk Assessment

The department completes its annual risk assessment as required under *Tennessee Code Annotated*, Section 9-18-101 using guidance provided by the Tennessee Department of Finance and Administration (F&A). The Department's November 2016 Financial Integrity Act Risk Assessment risks of non-compliance were assessed by compliance type requirement for the Department as a whole. For the December 2017 Financial Integrity Act Risk Assessment, based on revised F&A guidance, risks were assessed on a more programmatic/divisional level.

Auditor's Comment

Condition C:

This condition is not about management's resolution of a prior audit finding related to $56,824 of unallowable building costs but rather depreciation expense for the related building. Depreciation is recorded as an expense even though it is not a cash transaction. The subrecipient's records show that a portion of the depreciation expense for the building ***was*** incorrectly allocated to the Summer Food Service Program and thus questioned.

Finding Number	2017-013
CFDA Number	10.598, 84.126, 93.464, 93.558, 93.563, 93.575, 93.596, 93.667, and 93.778
Program Name	Supplemental Nutrition Assistance Program (SNAP) Recipient Trafficking Prevention Grants Rehabilitation Services - Vocational Rehabilitation Grants to States ACL Assistive Technology Temporary Assistance for Needy Families Cluster Child Support Enforcement Child Care and Development Fund Cluster Social Services Block Grant Medicaid Cluster
Federal Agency	Department of Agriculture Department of Education Department of Health and Human Services
State Agency	Department of Human Services
Federal Award Identification Number	2015S810621, 8044 H126A160063, 8044 H126A170063, 1701TNSGAT, G1502TNTANF, G1602TNTANF, 1604TNCSES, 1704TNCSES, G1601TNCCDF, G1501TNSOSR, G1601TNSOSR, 05-1605TN5ADM, and 05-1705TN5ADM
Federal Award Year	2015 through 2017
Finding Type	Significant Deficiency (84.126, 93.558, 93.563, 93.575, 93.596, and 93.778) Noncompliance
Compliance Requirement	Allowable Costs/Cost Principles
Repeat Finding	2016-014
Pass-Through Entity	N/A

Questioned Costs

CFDA	Federal Award Identification Number	Amount
10.598	2015S810621	$521,215
84.126	8044 H126A160063	$14,542
84.126	8044 H126A170063	$33,078
93.464	1701TNSGAT	$4,439
93.558	G1502TNTANF	$149,105
93.558	G1602TNTANF	$53,620
93.563	1604TNCSES	$16,183
93.563	1704TNCSES	$56,931
93.575	G1601TNCCDF	$358
93.667	G1501TNSOSR	$9,581
93.667	G1601TNSOSR	($4,288)
93.778	05-1605TN5ADM	$8,846
93.778	05-1705TN5ADM	$6,257

As noted in the prior two audits, fiscal staff for the Department of Human Services did not comply with federal requirements related to cost allocation plans, resulting in federal questioned costs of $869,867

Background

Because the Department of Human Services administers various public assistance programs, federal regulations require the state to submit a cost allocation plan that outlines the procedures used to identify, measure, and allocate costs to all programs administered by the department. Fiscal staff within the Department of Finance and Administration create and submit the cost allocation plan on behalf of the Department of Human Services, as well as allocate costs to federal grant awards in accordance with the cost allocation plan.

In accordance with federal regulations, fiscal staff allocate administrative costs that cannot be directly charged to a specific federal program to all benefitting federal programs based on the cost allocation plan. During the audit period, July 1, 2016, through June 30, 2017, two cost allocation plans were effective for the department. The first plan was effective July 1, 2016, through March 31, 2017. The second was effective April 1, 2017. A total of $381,213,289 of the department's expenditures during our audit period was subject to allocation under the cost allocation plan. (Federal regulations exclude from cost allocation plans expenditures for financial assistance, medical vendor payments, food stamps, and payments for services and goods provided directly to program recipients.)

According to Title 45, *Code of Federal Regulations* (CFR), Part 95, Section 507(a), a cost allocation plan for a state agency must describe the procedures used to identify, measure, and allocate all costs to each of the programs operated by the state agency.

Fiscal staff use activity codes in Edison, the state's accounting system, to track expenditures for the department's programs and activities. For each activity code, management generally includes in the cost allocation plan a brief description of the activity or program; identifies whether the costs for the activity are allocated to all programs, multiple programs, or one program; and identifies the basis that staff use to allocate costs for the activity.

Each quarter, fiscal staff prepare cost allocation tables. Generally, each table covers a specific activity that department staff perform for programs, identifies one or more federal programs to which costs for the activity should be charged, and identifies the percentage of costs associated with the specific activity that should be charged to each federal program.

Fiscal staff then use the cost allocation tables' percentages to prepare cost allocation spreadsheets that identify the amount of expenditures that fiscal staff should allocate to the federal programs administered by the department.

Finally, fiscal staff enter cost allocation entries into the department's accounting system based on the cost allocation calculations documented in the spreadsheets.

In the prior audit, we found that fiscal management did not amend the cost allocation plan to include new activity codes and allocated expenditures using methodologies that were inconsistent with the approved cost allocation plan. Department management concurred in part with the prior audit finding and stated, "The Department is currently in the process of revising the cost allocation plan . . . to take effect on April 1, 2017," and "A cost allocation manager position was created in December 2016 to oversee the Department's cost allocation processes. . . . The position is also responsible for ensuring the cost allocation plan is updated when required."

The Department Controller[16] submitted an amended cost allocation plan, effective April 1, 2017, and created a new accounting manager position to oversee the department's cost allocation processes which significantly reduced the amount of costs allocated improperly during the last quarter of the audit period. Despite these efforts, during the current audit, we found that fiscal staff still allocated expenditures using methodologies that were inconsistent with the department's approved cost allocation plan. In addition, we found that the department's amended cost allocation plan did not include all required information. As a result of the errors identified during the current audit, we questioned a net[17] total of $869,867 in federal costs and $328,323 in state matching costs.

Summary of Conditions

We tested fiscal staff's cost allocation processes for the periods October 1, 2016, to December 31, 2016, and April 1, 2017, to June 30, 2017. Based on testwork performed, the Department Controller did not ensure that the cost allocation plan adhered to federal regulations. Specifically, we noted that the Department Controller

- did not ensure that the amended cost allocation plan included all federally required information (see Condition A);
- did not ensure fiscal staff used allocation methodologies that were consistent with the approved cost allocation plan (see Condition B); and
- did not amend the cost allocation plan prior to changing allocation methodologies (see Condition C).

Condition A. The Department's Amended Public Assistance Cost Allocation Plan Did Not Include All Federally Required Information

Federal regulations require state agencies to include specific information in any public assistance cost allocation plan submitted for approval. Specifically, 45 CFR 95.507 identifies the information the state is required to include within the plan. As part of our audit procedures, we reviewed the department's amended *Public Assistance Cost Allocation Plan,* effective April 1, 2017, for compliance with 45 CFR 95.507 and determined that the Department Controller did not ensure that the amended cost allocation plan complied with federal regulations.

The Plan Did Not Include an Estimated Cost Impact Analysis

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[16] On April 11, 2016, the Department of Finance and Administration assumed responsibility for performing the Department of Human Services' fiscal functions, including preparing and implementing cost allocation plans. Therefore, the Department Controller and other fiscal employees referenced in this finding are employees within the Department of Finance and Administration.

[17] Due to the nature of the cost allocation process, errors generally result in overcharging certain federal programs and undercharging others. After netting overcharges against any undercharges for the same federal program, we questioned the net amount by which each federal program was overcharged.

The department's cost allocation plan is required to include the estimated cost impact resulting from the proposed changes to a previously approved plan. This estimated cost impact analysis should compare costs allocated using the proposed allocation methodology to costs allocated using the currently approved allocation methodology. Per federal regulations, if it is impractical to obtain the data needed to perform the analysis, "an alternative approach should then be negotiated with the Director, DCA [U.S. Department of Health and Human Services' Division of Cost Allocation], prior to submission of the cost allocation plan."

Based on our review, the Department Controller did not ensure the cost allocation plan included an estimated cost impact analysis, as required by federal regulations. We were also provided no indication that the Department Controller negotiated an alternative approach with the federal government prior to submitting the plan. Instead, the plan simply stated, "We do not anticipate that this PACAP will have any significant effect on DHS' [the Department of Human Services] claims for FFP [federal financial participation]."

Fiscal staff provided us an estimated cost impact analysis after the plan was submitted to the DCA for approval. This analysis was only for the period January 2017 through March 2017, and only for a small section of the department. Contrary to management's comments, the cost impact analysis indicated that the amended plan would have a significant impact on almost all federal programs included in the analysis. For example, under the amended plan, January 2017 through March 2017's allocated costs increased 277% for the Social Security Disability Insurance program and decreased 69% for the Child Support Enforcement program. See the table below for a summary of our results.

Table 1

Cost Impact Analysis for Amended Cost Allocation Plan

Program	Allocations Under Old Plan	Allocations Under New Plan	Difference	Percentage of Change
Child Care and Development Block Grant	$740,525	$1,002,497	$261,972	35%
Child Support Enforcement	1,385,010	435,893	(949,117)	(69%)
Community Services Block Grant	48,190	4,143	(44,047)	(91%)
Medical Assistance Program	1,177,531	222,757	(954,774)	(81%)
Social Security Disability Insurance	384,878	1,451,764	1,066,886	277%
Social Services Block Grant	278,011	487,459	209,448	75%
State Administrative Expenses for Child Nutrition	473,239	39,557	(433,682)	(92%)
Supplemental Nutrition Assistance Program	6,290,414	6,333,225	42,811	1%
Temporary Assistance for Needy Families	932,015	1,033,482	101,467	11%
Vocational Rehabilitation	1,033,451	1,732,485	699,034	68%

Due to the significant differences noted, as well as the lack of any additional analyses provided by fiscal management, we concluded that management's comment stating that it anticipated no significant effect on DHS's claims for FFP was unsupported. In addition, although we requested the supporting data behind the impact analysis management provided, management only provided the summary spreadsheet of the results and did not provide supporting data for the calculations. As a result, we could not review the underlying calculations to analyze the specific causes of the differences and determine whether the differences were the result of inequitable cost allocation practices. We also could not trace the amounts in the analysis to the department's cost allocation spreadsheets for the time period.

Finally, we concluded that the department did not appear to have established adequate controls over cost allocation, due to several weaknesses in the impact analysis, such as the following:

- Management included only one section of the department in the analysis even though the cost allocation plan included revisions that could impact other areas of the department differently. The departmental section included in the analysis made up $12,743,264 of the $96,419,509 in total expenditures subject to the cost allocation plan for the period January through March 2017.
- Management included only one quarter in the analysis even though a significant change in the amended cost allocation plan was based on an inaccurate assumption that overcharges to programs in one quarter would be reversed in the next quarter. See Finding 2017-010. A multi-period analysis would have allowed management to test the validity of this assumption.
- There was no evidence that management performed follow-up procedures for the significant variances in Table 1 above. Significant variances could be the result of inequitable allocation methods (meaning the plan would be in violation of federal cost principles) or errors in the impact analysis.
- The amount of expenditures included in the impact analysis did not agree with the department's cost allocation schedules for the period; therefore, it was not clear that the data used to prepare the analysis was reliable.

Criteria for Condition A

Regarding estimated costs, 45 CFR 95.507(b)(5) states that the cost allocation plan shall include

> The estimated cost impact resulting from the proposed changes to a previously approved plan. These estimated costs are required solely to permit an evaluation of the procedures used for identifying, measuring, and allocating costs. Therefore, approval of the cost allocation plan shall not constitute approval of these estimated costs for use in calculating claims for FFP. Where it is impractical to obtain this data, an alternative approach should then be negotiated with the Director, DCA, prior to submission of the cost allocation plan.

Cause for Condition A

When we asked the Department Controller why the analysis was excluded from the cost allocation plan, he stated that the regulations are ". . . clear that the analysis itself is not something that is approved as part of the cost allocation plan and is an estimate . . ." While the regulation quoted above does state that approval of the plan does not constitute approval of the costs in the estimated impact analysis, the regulation requires the estimated impact to be included.

Condition B. Fiscal Staff Used Cost Allocation Methods That Were Inconsistent With the Plan

For our audit period of July 1, 2016, through June 30, 2017, to determine if the department followed its approved cost allocation plan when charging costs to federal grants, we compared the Edison activity codes that fiscal staff used to charge expenditure costs to grants with all combinations of activity codes included in the department's cost allocation plan. For the period July 1, 2016, through March 31, 2017, the cost allocation plan included 378 activity codes. For the period April 1, 2017, through June 30, 2017, the cost allocation plan did not contain a listing of activity codes, but fiscal staff provided us with a listing of activity codes used during the period and information regarding how those codes' costs were allocated. This listing included 136 unique codes. We specifically wanted to determine whether the department included all activities in the cost allocation plan and allocated costs according to the plan. Testwork was performed to determine this for both cost allocation plans effective during the year.

For the period July 1, 2016, through March 31, 2017, the cost allocation plan details how costs will be allocated by providing activity codes and cost allocation methods for each activity code. While each activity code in the plan is associated with no more than one underlying activity, there are many instances where one activity is associated with multiple activity codes. (For example, DHS may have submitted only one activity code for the Vocational Rehabilitation program in its plan, but staff actually used multiple activity codes for the program to provide for a greater level of detail in accounting records.) For the period of April 1, 2017, through June 30, 2017, the listing provided by fiscal staff provided this information.

As a result, in order to determine whether costs for the activity codes were allocated in accordance with the approved cost allocation plan, we first determined whether each activity code had a related activity description included in the plan.

If the activity description was included in the plan, we then determined whether fiscal staff used the allocation method described in the plan for that description.

Based on our review, we found that the Department Controller did not ensure that the department's cost allocation plan included all activity codes or that costs were allocated to programs according to the methodologies in the approved cost allocation plan.

July 1, 2016, Through March 31, 2017: All Activity Codes Were Not Included in the Plan and Costs Were Not Always Allocated in Accordance With the Plan

Codes not included but allocation methodologies were consistent with methodologies for included activities

For the period July 1, 2016, through March 31, 2017, the Department Controller did not ensure the cost allocation plan included 182 activity codes the department used in the state's accounting system, Edison, to allocate costs. Expenditures charged to these 182 activity codes totaled $86,091,223. See Table 2 for the total expenditures charged to each federal program.

Table 2
Expenditures (by Program) Charged to Activity Codes Not Included in the Approved Cost Allocation Plan, July 1, 2016, Through March 31, 2017

Program	Federal Expenditures	Non-Federal Expenditures	Total Expenditures
Assistive Technology	$148,765	$ -	$148,765
Child and Adult Care Food Program	15,451,228	-	15,451,228
Child Care and Development Block Grant	191,323	409,840	601,163
Community Services Block Grant	3,629	-	3,629
Child Support Enforcement	1,033,056	544,485	1,577,541
Child Support Enforcement Research	22,655	-	22,655
Independent Living Services for Older Individuals Who Are Blind	936,865	93,318	1,030,183
Independent Living State Grants	28,792	3,199	31,991
Medical Assistance Program	995,529	1,075,768	2,071,297
Maternal and Child Health Services Block Grant	16,708	16,707	33,415
State Administrative Expenses for Child Nutrition	30,403	-	30,403
Summer Food Service Program	8,636,177	-	8,636,177
Supplemental Nutrition Assistance Program	8,828,069	6,057,165	14,885,234
SNAP Recipient Trafficking Prevention Grants	521,215	-	521,215
Social Services Block Grant	141,561	-	141,561
Social Security Disability Insurance	235,911	-	235,911
Temporary Assistance for Needy Families	7,427,276	3,706,260	11,133,536
Vocational Rehabilitation	20,520,115	5,289,442	25,809,557
Vocational Rehabilitation Unit In-Service Training	2,074	231	2,305
State Only Activities*	-	3,723,457	3,723,457
Totals	**$65,171,351**	**$20,919,872**	**$86,091,223**

Source: Summarized using accounting records from Edison, the state's accounting system.
* "State Activities" refers to expenditures funded using state funds that were not recorded in the accounting system as matching expenditures for federal programs or expenditures used to meet level of effort requirements for federal programs.

For 172 of these 182 activity codes, we found that even though fiscal staff had not included an activity code in the cost allocation plan (either in the original submission or through amendments), fiscal staff allocated costs associated with the 172 activity codes in the same manner as (or similarly to) other similar program activities which had been included and approved in the plan. Because we found these allocations methods consistent with the plan, we did not question costs even though the activity codes were not technically approved in the plan.

Codes not included and allocation methodologies were inconsistent with methodologies for included activities

Although we found that 172 of 182 activity codes for the period of July 1, 2016, through March 31, 2017, were allocated consistently with the approved cost allocation plan, we found that the department's fiscal staff allocated expenditures for the remaining 10 activity codes using methodologies that were inconsistent with any of the approved allocation methodologies identified in the cost allocation plan for similar activities. Specifically, we noted the following:

a. For one activity, the Medical Evaluation Unit, the cost allocation plan required costs to be treated as direct charges to the Medicaid Cluster; however, we found that all $433,158 in expenditures for this activity were charged to TANF. These costs are included in Table 3 below.

b. For one activity, the Tennessee Technology Access Project Director, the cost allocation plan required the department to charge costs to federal programs as direct costs, with supporting documentation demonstrating the proportion of benefits provided to federal programs (such as timesheets). Fiscal staff allocated $8,877 split between the Assistive Technology and Vocational Rehabilitation grants using a predetermined percentage, rather than allocating costs based on a timesheet or some other supporting documentation. Since the department did not use a valid methodology to allocate these costs, we questioned the costs. These costs are included in Table 3 below.

c. For the remaining eight activity codes, totaling $2,075,935 in expenditures, the approved cost allocation plan required fiscal staff to treat the costs as indirect costs. Specifically, fiscal staff were required to allocate the activities' costs to all programs administered by the department based on the number of each program's full-time equivalent staff or by the results of random moment time sampling systems. Instead of allocating the costs to *all* programs using these bases, we found that fiscal staff allocated costs for the eight activity codes to three or fewer programs, depending on the activity code. We calculated the correct allocation amounts and compared our calculations to fiscal staff's allocations. We questioned the differences. These amounts are included in Table 3 below.

Table 3
Differences (by Program) for Ten Activity Codes Not Charged in Accordance With the Cost Allocation Plan for the Period July 1, 2016, Through March 31, 2017

Program	Federal Expenditures	State Expenditures	Total Expenditures
Programs Overcharged			
Assistive Technology	$4,439	$ -	$4,439
Child Care and Development Block Grant	-	58,020	58,020
Child Support Enforcement	73,089	37,653	110,742
Medical Assistance Program	15,086	15,086	30,172
SNAP Trafficking Prevention Program	521,215	-	521,215
Social Services Block Grant	5,265	-	5,265
Temporary Assistance for Needy Families	202,677	198,952	401,630
Vocational Rehabilitation	47,499	12,978	60,476
Total	**$869,270**	**$322,689**	**$1,191,959**

Programs Undercharged			
Child and Adult Care Food Program	(38)	-	(38)
Community Service Block Grant	(604)	-	(604)
Independent Living for Older Persons Who Are Blind	(11,300)	(1,256)	(12,556)
Social Security Disability Insurance	(156,975)	-	(156,975)
State Administrative Expenses for Child Nutrition	(4,722)	-	(4,722)
Summer Food Service Program	(11)	-	(11)
Supplemental Nutrition Assistance Program	(287,509)	(287,509)	(575,018)
Total	**(461,159)**	**(288,765)**	**(749,924)**

April 1, 2017, Through June 30, 2017: Costs Were Not Allocated in Accordance With the Plan

We found that 6 activity codes for the period of April 1, 2017, through June 30, 2017, were not allocated consistently with the approved cost allocation plan. Specifically, the approved cost allocation plan required fiscal staff to allocate the activities' costs to all programs administered by the department based on the number of each program's filled full- and part-time positions at the end of the prior quarter. Instead of allocating the costs to all programs, we found that fiscal staff charged the costs for the six activity codes to one or more programs, but not all programs. Since the activities were excluded from the plan and charged to programs in a manner inconsistent with the cost allocation plan, we questioned the costs allocated to these activity codes. See Table 4 below.

Table 4
Expenditures (by Program) Charged to Activity Codes Inconsistent With the Cost Allocation Plan, April 1, 2017, Through June 30, 2017

Program	Federal Expenditures	State Expenditures	Total Expenditures
Child Care and Development Block Grant	$358	$5,523	$5,881
Child Support Enforcement	25	13	38
Independent Living Services for Older Individuals Who Are Blind	1	-	1
Medical Assistance Program	17	17	34
Supplemental Nutrition Assistance Program	281	281	562
Social Services Block Grant	28	-	28
Social Security Disability Insurance	125	-	125
Temporary Assistance for Needy Families	48	48	96
Vocational Rehabilitation	121	33	154
Totals	**$1,004**	**$5,915**	**$6,919**

Source: Summarized using accounting records from Edison, the state's accounting system.

Criteria for Condition B

According to 45 CFR 95.507(b)(4), the state's cost allocation plan must include

> the procedures used to identify, measure, and allocate all costs to each benefiting program and activity (including activities subject to different rates of FFP [federal financial participation—the federal government's share of expenditures made by a state agency for public agency programs]).

In addition, 45 CFR 95.509 requires the state to promptly amend the cost allocation plan and submit the amended plan to the U.S. Department of Health and Human Services if

> changes occur which make the allocation basis or procedures in the approval [*sic*] cost allocation plan invalid.

According to 45 CFR 95.519,

> If costs under a Public Assistance program are not claimed in accordance with the approved cost allocation plan (except as otherwise provided in §95.517), or if the State failed to submit an amended cost allocation plan as required by §95.509, the costs improperly claimed will be disallowed.

Finally, 2 CFR 200 (and 45 CFR 75), Appendix VI, Section C, states,

> State public assistance agencies will develop, document and implement . . . public assistance cost allocation plans in accordance with Subpart E of 45 CFR Part 95. The plan will include all programs administered by the state public assistance agency.

According to the amended cost allocation plan's approval letter provided to the department by the U.S. Department of Health and Human Services, approval of the plan is based on information provided by the state and is void if the information is later found to be materially incomplete or inaccurate.

Cause for Condition B

Fiscal staff made changes to the cost allocation methodologies used but did not revise the cost allocation plan to reflect these changes until the revision of the cost allocation plan effective April 1, 2017. After the cost allocation plan was amended, fiscal staff removed activity codes that were no longer used from their cost allocation workbooks. Small amounts of expenditures were still charged to these activity codes and therefore were not properly allocated in accordance with the new plan.

Condition C. Fiscal Staff Did Not Amend the Cost Allocation Plan Prior to Changing Allocation Methodologies

Based on our testwork, fiscal staff did not amend the cost allocation plan prior to revising cost allocation methodologies, which is not in accordance with federal requirements.

Position Counts Cost Allocation Basis

According to the amended cost allocation plan, effective April 1, 2017, departmental divisions whose costs are allocated using the position counts basis must be allocated using counts of full- and part-time positions at the end of the prior quarter. Based on our review of fiscal staff's cost allocation tables, for costs incurred April 1, 2017, through June 30, 2017, all cost allocation tables using this basis were prepared using average filled position counts for the quarter January 2017 through March 2017, rather than filled positions as of March 31, 2017. As noted in Finding 2017-010, we questioned costs due to fiscal staff using January 2017 through March 2017 information to allocate the department's April 2017 through June 2017 costs; thus, the only additional issue noted here is that fiscal staff were required to use position counts as of the end of the prior quarter, but fiscal staff used average filled position counts instead. We did not question costs related to this matter, because the information needed to calculate questioned costs was not readily available; however, we noted that using average filled position counts for a quarter would provide a more accurate determination of the proportional benefits programs received throughout the quarter. Prior to using the revised method, however, federal regulations required the Department Controller to submit an amendment to the department's approved cost allocation plan.

Assistant Commissioner of Community and Social Services

According to the Cost Allocation Plan effective for the period July 2014 through March 2017, the Assistant Commissioner of Community and Social Services and the Assistant Commissioner's staff should be allocated using Table 13. This table is made using position counts for staff working on the Child Care and Development Fund, Community Services Block Grant, Adult Protective Services, and the State Administrative Expenses for Child Nutrition (SAE) programs. Beginning October 2016, the department reorganized management's responsibilities, and this position lost purview over the SAE program. The department created Table 18 to more accurately allocate this Assistant Commissioner's costs. Even though this is a more accurate allocation basis, the fiscal staff did not amend the cost allocation plan before this reorganization occurred. The department ultimately updated the cost allocation plan which included these changes and obtained approval from the federal agency effective April 2017. Although fiscal staff did not claim costs in accordance with its approved cost allocation plan for October 2016 through March 2017, we did not question costs due to the failure to claim costs in accordance with the cost allocation plan, because charging costs to the SAE program in accordance with the plan would have been a violation of federal requirements. This is because SAE did not receive any benefit from the Assistant Commissioner's Office's activities during this period.

Cause for Condition C

Fiscal staff were not aware that the cost allocation plan needed to be amended before new methodologies could be placed into practice. For the positions count basis, fiscal staff continued to use the previous methodology, not realizing that the amended cost allocation plan no longer permitted using average position counts to create cost allocation tables.

Criteria for Condition C

Concerning amending the cost allocation plan, 45 CFR 95.509(a) states that the state shall promptly amend the cost allocation plan and submit the amended plan for approval if any of the following events occur:

> (1) The procedures shown in the existing cost allocation plan become outdated because of organizational changes, changes in Federal law or regulations, or significant changes in program levels, affecting the validity of the approved cost allocation procedures.
>
> (2) A material defect is discovered in the cost allocation plan by the Director, DCA [U.S. Department of Health and Human Services' Division of Cost Allocation] or the State.
>
> (3) The State plan for public assistance programs is amended so as to affect the allocation of costs.
>
> (4) Other changes occur which make the allocation basis or procedures in the approval cost allocation plan invalid.

According to 45 CFR 95.517(a) "A State must claim FFP [federal financial participation] for costs associated with a program only in accordance with its approved cost allocation plan." This requirement is effectively extended to all programs administered by state public assistance agencies by Section C, Appendix VI, of 2 CFR 200 (formerly Section C of OMB A-87, Attachment D), which states,

> State public assistance agencies will develop, document and implement, and the Federal Government will review, negotiate, and approve, public assistance cost allocation plans in accordance with Subpart E of 45 CFR Part 95. The plan will include all programs administered by the state public assistance agency.

Condition D: Risk Assessment

Given the problems identified during our fieldwork, we also reviewed the Department of Human Services' November 2016 Financial Integrity Act Risk Assessment and determined that top management assessed the risk that "Costs charged to a federal program are not allowable under program regulations" as having a remote likelihood and small impact; however, management did not identify any mitigating controls related to the issue. Given the unallowable costs and cost principles issues identified in this finding and others during the current audit, such as 2017-015, 2017-033, and 2017-037, we concluded that management should have assessed the likelihood as reasonably possible, assessed the impact as large, and included a control activity to mitigate the risk in the department's annual risk assessment.

Effect for All Conditions

Failure to allocate costs in accordance with the cost allocation plan and federal requirements increases the risk that fiscal staff will not assign an appropriate share of costs to programs and that federal grantors will disallow costs charged to federal programs.

Additionally, federal regulations address actions that federal agencies may impose in cases of noncompliance. As noted in 2 CFR 200.338, "If a non-Federal entity fails to comply with Federal statutes, regulations or the terms and conditions of a Federal award, the Federal awarding agency or pass-through entity may impose additional conditions," including, as described in Section 200.207, "Specific conditions":

> (1) Requiring payments as reimbursements rather than advance payments;
>
> (2) Withholding authority to proceed to the next phase until receipt of evidence of acceptable performance within a given period of performance;
>
> (3) Requiring additional, more detailed financial reports;
>
> (4) Requiring additional project monitoring;
>
> (5) Requiring the non-Federal entity to obtain technical or management assistance; or
>
> (6) Establishing additional prior approvals.

Furthermore, Section 200.338 also states,

> If the Federal awarding agency or pass-through entity determines that noncompliance cannot be remedied by imposing additional conditions [as described above], the Federal awarding agency or pass-through entity may take one or more of the following actions, as appropriate in the circumstances:
>
> (a) Temporarily withhold cash payments pending correction of the deficiency by the non-Federal entity or more severe enforcement action by the Federal awarding agency or pass-through entity.
>
> (b) Disallow (that is, deny both use of funds and any applicable matching credit for) all or part of the cost of the activity or action not in compliance.
>
> (c) Wholly or partly suspend or terminate the Federal award.
>
> (d) Initiate suspension or debarment proceedings as authorized under 2 CFR part 180 and Federal awarding agency regulations (or in the case of a pass-through entity, recommend such a proceeding be initiated by a Federal awarding agency).
>
> (e) Withhold further Federal awards for the project or program.
>
> (f) Take other remedies that may be legally available.

<u>Questioned Costs</u>

We questioned a total of $1,198,190 due to the net amount of overcharges to federal programs, consisting of federal questioned costs of $869,867 and $328,323 in questioned costs related to state matching funds for federal grant awards. See Tables 3 and 4 above for details regarding all overcharges and undercharges.

This finding, in conjunction with findings 2017-010, 2017-012, 2017-014, 2017-015, 2017-037, and 2017-040 (which also included federal questioned costs for the federal compliance requirement Allowable Costs/Cost Principles), results in total known federal questioned costs exceeding $25,000 for a type of compliance requirement for two federal programs. This finding, in conjunction with findings 2017-012, 2017-014, and 2017-015, results in total known federal questioned costs exceeding $25,000 for a program which is not audited as a major program.

Regarding questioned costs, 2 CFR 200.516(a)(3) requires us to report known questioned costs that are greater than $25,000 for a type of compliance requirement for a major program. Additionally, 2 CFR 200.516(a)(4) requires us to report known questioned costs that are greater than $25,000 for a federal program which is not audited as a major program.

According to 2 CFR 200.84,

> *Questioned cost* means a cost that is questioned by the auditor because of an audit finding:
>
> (a) Which resulted from a violation or possible violation of a statute, regulation, or the terms and conditions of a Federal award, including for funds used to match Federal funds;
>
> (b) Where the costs, at the time of the audit, are not supported by adequate documentation; or
>
> (c) Where the costs incurred appear unreasonable and do not reflect the actions a prudent person would take in the circumstances.

Recommendation

The Department Controller should establish adequate internal controls over the cost allocation plan amendment process, including addressing each of the deficiencies identified above. The Department Controller should also ensure that the Department of Human Services' cost allocation plan contains all required information, fiscal staff's accounting practices for cost allocation are consistent with the approved cost allocation plan, and that the cost allocation plan is amended prior to fiscal staff implementing any new cost allocation methodology.

The Commissioner of the Department of Human Services should assess all significant risks with sufficient attention to the impact and likelihood of the risk. The risk assessment and the mitigating controls should be adequately documented and approved by the Commissioner, who should implement effective controls to ensure compliance with applicable requirements, assign employees to be responsible for ongoing monitoring of the risks and any mitigating controls, and take action if deficiencies occur.

Management's Comment

We concur in part.

Condition A. The Department's Amended Public Assistance Cost Allocation Plan Did Not Include All Federally Required Information

We do not concur.

The cost impact statement was not included in the original transmission of the cost allocation plan; however, it was provided to our federal partners during the negotiation phase of the process. The statement in the cost allocation plan was based on overall effect to federal programs as opposed to analysis of each individual program since the document itself is all encompassing. As the citation in the finding indicates, the cost impact statement is an estimate and the approval of the plan does not constitute an approval of the estimate.

Condition B. Failure to Use Cost Allocation Methods Consistent With the Plan

We concur in part.

The department concurs that not all codes were included in the 2014 cost allocation plan. This is one of the reasons the cost allocation plan was amended April 1, 2017. The updated plan reduces the complexities and risk for error.

In regard to the 10 omitted codes, where the captured and properly allocable costs were allocated using methodologies not specifically prescribed by the cost allocation plan, an important consideration is that while the 10 activity codes noted in the finding may not have been charged in accordance with (or consistent with) the approved plan, the costs were in fact properly charged to the benefiting objectives. Specifically,

a.) The Medical Evaluation Unit previously processed cases for Temporary Assistance for Needy Families (TANF) as well as Medicaid. For state fiscal year 2017, the unit only handled TANF cases; therefore, costs were charged to TANF, the benefiting program.

b.) The Tennessee Technology Access Project Director's costs were initially (by speedchart) recorded using a predefined percentage. The director kept a timesheet outside of the system so that fiscal staff could reallocate her time based on direct charges. Journal entries to charge the director's time were made throughout the audit period and covered the period July 1, 2016, through April 16, 2017, at which time Edison functionality was added so that the director could keep her time in the system.

c.) For the remaining 8 activity codes, the allocation methodologies used to charge the benefitting programs are shown in the table below:

Dept	Program	Unit	Allocation Basis	Program
3450103200		OLPD Child Support (1)	Direct	100% Child Support
3450103300		OLPD Family Assistance (1)	RMS	100% Family Assistance (Table FA-2)
3450103400		OLPD Child Care (1)	Total Costs	100% Child Care (Table 8)
3450103500		OLPD Adult Protective Services (1)	Direct	100% APS
3450103600		OLPD Rehab Services (1)	Direct	100% VR
3450103600	701000	OLPD Rehab Services (1)	Direct	100% VR
3450103700		OLPD DDS (1)	Direct	100% DDS
3450105100	320001	SNAP Trafficking (2)	Direct	100% SNAP Trafficking Program

(1) While the cost allocation plan indicates that OLPD costs would be treated as indirect costs, costs were allocated as direct costs to the benefiting objectives for 4 of the 6 Department

IDs (2 lines above have the same department ID), which is believed to be more accurate. OLPD staff in each area work solely on the benefiting objectives for which they were charged. For OLPD staff benefiting Family Assistance and Child Care, the costs were allocated using the same methodology that is used to allocate other staff in those areas of responsibility.

(2) The SNAP trafficking costs were allocated as direct SNAP trafficking charges.

In regard to the 6 activity codes for the period April 1, 2017, through June 30, 2017, these charges occurred during the accounting adjustment periods to close the state's books (after June 30, 2017). These charges were allocated in a manner closely mirroring allocated charges based on Table 1. Several programs the department administers are small in relation to the others (less than 1% to be charged based on Table 1), that they cannot be included in the established speed chart based allocation process. The system will not accept a line item in the speed chart for less than 1%. Management believes the alternative allocation approach utilized in this particular situation resulted in an equitable allocation. The costs presented in Table 4 appear to be all costs charged via the speed chart and not the immaterial difference between the speed chart allocation percentages and Table 1.

Condition C. Fiscal Staff Did Not Amend the Cost Allocation Plan Prior to Changing Allocation Methodologies

We concur.

The plan was not amended prior to revising cost allocation methodologies; however, as noted by the state auditors, the methodologies resulted in the equitable distribution of costs to the proper benefitting programs. A revised cost allocation plan was submitted on April 1, 2017, which resolved the issues noted in Condition C.

Condition D. Risk Assessment

The department completes its annual risk assessment as required under *Tennessee Code Annotated*, Section 9-18-101, using guidance provided by the Tennessee Department of Finance and Administration (F&A). For the Department's November 2016 Financial Integrity Act Risk Assessment, risks of non-compliance were assessed by compliance type requirement for the Department as a whole. For the December 2017 Financial Integrity Act Risk Assessment, based on revised F&A guidance, risks were assessed on a more programmatic/divisional level.

Auditor's Comment

Condition A. The Department's Amended Public Assistance Cost Allocation Plan Did Not Include All Federally Required Information

Federal regulations required the estimated impact to be included in the plan, and management acknowledges that "The cost impact statement was not included in the original transmission of the cost allocation plan"; therefore, it is not clear why management has not concurred with Condition A. If the department was unable to obtain the necessary data to prepare the estimate, federal regulations require the department to negotiate an alternative approach "prior to submission of the plan." There is no provision for submitting the cost allocation plan first without the required estimated cost impact.

Finding Number	2017-014
CFDA Number	10.558, 10.560, 10.561, 84.126, 84.177, 93.558, 93.563, 93.569, 93.575, 93.667, 93.778, and 96.001
Program Name	Child and Adult Care Food Program State Administrative Expenses for Child Nutrition Supplemental Nutrition Assistance Program Cluster Rehabilitation Services - Vocational Rehabilitation Grants to States Rehabilitation Services - Independent Living Services for Older Individuals Who are Blind Temporary Assistance for Needy Families Cluster Child Support Enforcement Community Services Block Grant Child Care and Development Fund Cluster Social Services Block Grant Medicaid Cluster Disability Insurance/Supplemental Security Income Cluster
Federal Agency	Department of Agriculture Department of Education Department of Health and Human Services Social Security Administration
State Agency	Department of Human Services
Federal Award Identification Number	201616N109945, 201616N253345, 201717N253345, 201616IS251445, 201717IS251445, 8044 H126A160063, 8044 H126A170063, H177B160064, H177B170064, G1402TNTANF, G1502TNTANF, G1602TNTANF, 1604TNCSES, 1704TNCSES, G15B1TNCOSR, G16B1TNCOSR, G1701TNCCDF, G1501TNSOSR, G1601TNSOSR, 05-1605TN5ADM, 05-1705TN5ADM, 8826 04-16-04TNDI00, and 8826 04-17-04TNDI00
Federal Award Year	2014 through 2017
Finding Type	Significant Deficiency (10.558, 10.561, 84.126, 93.558, 93.563, and 93.575) Noncompliance
Compliance Requirement	Allowable Costs/Cost Principles
Repeat Finding	2016-015
Pass-Through Entity	N/A
Questioned Costs	

CFDA	Federal Award Identification Number	Amount
10.558	201616N109945	$4,765
10.560	201616N253345	$12,615
10.560	201717N253345	$9,881
10.561	201616IS251445	$111,565
10.561	201717IS251445	$158,424
84.126	8044 H126A160063	$44,738
84.126	8044 H126A170063	$62,849

84.177	H177B160064	$1,701
84.177	H177B170064	$2,568
93.558	G1402TNTANF	$4,933
93.558	G1502TNTANF	$3,895
93.558	G1602TNTANF	$57,358
93.563	1604TNCSES	$100,308
93.563	1704TNCSES	$132,192
93.569	G15B1TNCOSR	$6,875
93.569	G16B1TNCOSR	$4,670
93.575	G1701TNCCDF	$13,492
93.667	G1501TNSOSR	$11,993
93.667	G1601TNSOSR	$757,956
96.001	8826 04-16-04TNDI00	$16,522
96.001	8826 04-17-04TNDI00	$21,699

As noted in the prior two audits, fiscal staff for the Department of Human Services did not allocate costs in accordance with the department's approved cost allocation plan, resulting in federal questioned costs of $1,540,999

Background

Because the Department of Human Services (the department) administers various public assistance programs, federal regulations require the state to submit a cost allocation plan that outlines the procedures used to identify, measure, and allocate costs to all programs administered by the department. Fiscal staff within the Department of Finance and Administration create and submit the cost allocation plan on behalf of the Department of Human Services, as well as allocate costs to federal grant awards in accordance with the cost allocation plan.

In accordance with federal regulations, fiscal staff allocate administrative costs that cannot be directly charged to a specific federal program to all benefitting federal programs based on the cost allocation plan. During the audit period, July 1, 2016, through June 30, 2017, two cost allocation plans were effective for the department. The first plan was effective July 1, 2016, through March 31, 2017. The second was effective April 1, 2017. A total of $381,213,289 of the department's expenditures during our audit period was subject to allocation under the cost allocation plan. (Federal regulations exclude from cost allocation plans expenditures for financial assistance, medical vendor payments, food stamps, and payments for services and goods provided directly to program recipients.)

According to Title 45, *Code of Federal Regulations*, Part 95, Section 507(a), a cost allocation plan for a state agency must describe the procedures used to identify, measure, and allocate all costs to each of the programs operated by the state agency.

Each quarter, fiscal staff prepare cost allocation tables. Generally, each table covers a specific activity that department staff perform for programs, identifies one or more federal programs to which costs for the activity should be charged, and identifies the percentage of costs associated with the specific activity that should be charged to each federal program.

Fiscal staff then use the cost allocation tables' percentages to prepare cost allocation spreadsheets that identify the amount of expenditures that fiscal staff should allocate to the federal programs administered by the department.

Finally, fiscal staff enter cost allocation entries into the department's accounting system based on the cost allocation calculations documented in the spreadsheets.

In the prior audit, we found that fiscal management did not prepare cost allocation tables correctly, did not perform cost allocation entries, and used the incorrect cost allocation tables to allocate costs. Department management concurred in part with the prior audit finding and stated, "The Department is currently in the process of revising the cost allocation plan to take effect on April 1, 2017," and "A cost allocation manager position was created in December 2016 to oversee the Department's cost allocation processes. . . . The position is also responsible for ensuring the cost allocation plan is updated when required."

The Department Controller[18] submitted an amended cost allocation plan, effective April 1, 2017, and created a new accounting manager position to oversee the department's cost allocation processes, which significantly reduced the amount of costs allocated improperly during the last quarter of the audit period. Despite these efforts, during the current audit, we found that fiscal staff still did not prepare all cost allocation tables correctly, did not detect errors in cost allocation workbooks, used incorrect allocation tables, and did not always perform cost allocation entries. As a result of the errors identified during the current audit, we questioned a net[19] total of $1,540,999 in federal costs.

Summary of Conditions

We tested fiscal staff's cost allocation processes for the periods October 1, 2016, to December 31, 2016, and April 1, 2017, to June 30, 2017. Based on our testwork, we found that the Department Controller did not ensure fiscal staff allocated costs to federal awards in accordance with the cost allocation plan. Specifically, we noted that fiscal staff

- prepared three cost allocation tables incorrectly (see Condition A),
- did not detect errors in cost allocation workbooks for four areas (see Condition B), and
- used incorrect cost allocation tables to allocate costs for one area (see Condition C).

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[18] On April 11, 2016, the Department of Finance and Administration assumed responsibility for performing the Department of Human Services' fiscal functions, including preparing and implementing cost allocation plans. Therefore, the Department Controller and other fiscal employees referenced in this finding are employees within the Department of Finance and Administration.

[19] Due to the nature of the cost allocation process, errors generally result in overcharging certain federal programs and undercharging others. After netting overcharges against any undercharges for the same federal program, we questioned the net amount by which each federal program was overcharged.

Condition and Cause

Condition A. Fiscal Staff Prepared Three Cost Allocation Tables Incorrectly

Based on our testwork, fiscal staff prepared cost allocation tables CR-1, 9A-2, and ACS-3 incorrectly.

Table CR-1

Per the cost allocation plan effective from July 1, 2016, through March 31, 2017, fiscal staff created Table CR-1 to allocate all rent and office expenses related to the Citizen's Plaza State Office Building. The plan stated that these costs would be allocated based on square footage. The plan also stated that occupancy reports obtained from facility records would be used as the data to support the square footage allocation methodology. However, instead of using occupancy reports to identify the amount of square footage associated with each program, fiscal staff created Table CR-1 based on a count of full-time personnel assigned to each federal program.

Since fiscal staff did not prepare Table CR-1 based on square footage for the period July 1, 2016, through March 31, 2017, as required by the applicable plan, we questioned all costs allocated via Table CR-1 during the period. This resulted in $674,737 in federal questioned costs and $499,460 in questioned costs related to state matching funds. These questioned costs are included in **Table 1** below.

In accordance with the amended cost allocation plan, effective April 1, 2017, fiscal staff no longer use this table. Instead, effective April 1, 2017, fiscal management began allocating rent and office expenses to all programs based on full- and part-time position counts in accordance with the amended cost allocation plan. Because the costs are no longer required to be allocated based on square footage, we do not anticipate that this problem will reoccur.

Table 9A-2

Per the cost allocation plan effective from July 1, 2016, through March 31, 2017, fiscal staff created Table 9A-2 to allocate all expenses related to the Tech Support section. The plan stated that Tech Support costs would be allocated based on device counts (the number of devices assigned to department staff). The plan also stated that the department would use its inventory records to support the device count allocation methodology. We found that fiscal staff did not create Table 9A-2 using inventory records or any other information related to the number of devices. Instead of counting the number of devices associated with staff assigned to each program, fiscal staff created Table 9A-2 based on the number of full time personnel assigned to each program.

Since fiscal staff did not prepare Table 9A-2 based on device counts for the period July 1, 2016, through March 31, 2017, as required by the applicable plan, we questioned all costs allocated via Table 9A-2 during the period. This resulted in $165,010 in federal questioned costs and $136,511 in questioned costs related to state matching funds. These questioned costs are included in **Table 1** below.

In accordance with the amended cost allocation plan, effective April 1, 2017, fiscal staff no longer use this table. Instead, effective April 1, 2017, fiscal management began allocating Tech Support costs to all programs based on full- and part-time position counts in accordance with the amended cost allocation plan. Because the costs are no longer required to be allocated based on device counts, we do not anticipate that this problem will reoccur.

Table ACS-3

In accordance with both cost allocation plans effective during the audit period, fiscal staff created Table ACS-3 to allocate all costs associated with the department's Adult Protective Services (APS) division. According to the plans, APS' costs are allocated based on random moment sampling time studies. These studies involve randomly selecting APS employees to answer telephone surveys periodically throughout their workday to determine what program they are working on. The surveys allow the employees to choose between the Medical Assistance Program (Medicaid), the Social Services Block Grant (SSBG), or non-program related general administrative tasks. Since costs associated with administrative tasks cannot be allocated directly to one program, they should be split between Medicaid and SSBG proportionately.

Instead, fiscal staff assigned all costs related to administrative activities solely to SSBG. This means that for the period of July 1, 2016, through June 30, 2017, fiscal staff were charging the SSBG program costs that should have been allocated to Medicaid.[20] During this period, fiscal staff allocated $9,672,324 of expenditures through Table ACS-3. We recalculated Table ACS-3 to allocate administrative costs to both SSBG and Medicaid for the two quarters selected in our testwork—October 2016 through December 2016, and April 2017 through June 2017. For these two quarters, this error resulted in federal questioned costs of $148,060 for the SSBG program, while Medicaid was undercharged the same. These questioned costs are included in **Table 1** below.

Table 1
Combined Questioned Costs for Condition A

Program	Federal Expenditures	State Expenditures	Total Expenditures
Amount Overcharged			
Child and Adult Care Food Program	$ 4,765	$ -	$ 4,765
Child Care and Development Block Grant	-	112,409	112,409
Child Support Enforcement	232,045	119,538	351,583
Community Services Block Grant	11,545	-	11,545
Independent Living Services for Older Individuals Who Are Blind	4,269	474	4,743
Social Security Disability Insurance	38,221	-	38,221
Social Services Block Grant	178,502	-	178,502
State Administrative Expenses for Child Nutrition	35,988	-	35,988
Supplemental Nutrition Assistance Program	283,977	283,977	567,954

[20] Although requested, fiscal staff did not provide us any program-specific regulations for Medicaid that indicated that these administrative costs were prohibited from being charged to Medicaid.

Temporary Assistance for Needy Families	69,099	69,099	138,198
Vocational Rehabilitation	107,580	28,658	136,238
Total	**$965,991**	**$614,155**	**$1,580,146**
Amount Undercharged			
Medical Assistance Program	$(52,215)	$(52,215)	$(104,430)
Total	**$(52,215)**	**$(52,215)**	**$(104,430)**

Cause for Condition A

For Tables 9A-2 and CR-1, we concluded that the issues were primarily caused by the Department Controller and fiscal staff choosing not to change their cost allocation methodologies for the above areas until the cost allocation plan was amended. The Department Controller had started updating the cost allocation plan during our fieldwork for the prior Single Audit, and it was amended shortly after we released the prior audit report, which remedied these issues going forward. Additionally, for Table ACS-3, fiscal staff did not realize that, unless prohibited by program-specific federal regulations, administrative tasks that benefit multiple programs should be allocated to each program, not just SSBG.

Condition B. Fiscal Staff Did Not Detect Errors in Cost Allocation Workbooks for Four Areas

Appeals and Hearings

Based on our testwork, we found that the department allocated all Child and Adult Food Program (CACFP) costs incurred by the Appeals and Hearings division to the Child Care and Development Fund (CCDF) program due to a spreadsheet error. This issue was present during the period of July 1, 2016, through June 30, 2017. After we brought this matter to the attention of fiscal management, management addressed the matter promptly by recalculating allocation results for the division, correcting the erroneous workbook, and entering a correcting journal entry in the department's accounting records to resolve the error.

Because the department's controls were not sufficient to identify and correct the error and because management did not correct the error until after the audit period, we questioned costs related to the overcharges to CCDF and undercharges to CACFP. In total, CCDF was overcharged by $13,492, and CACFP was undercharged by an equal amount. The questioned costs are included in **Table 2** below.

Adult Protective Services – Tables 1 and 4

Based on our review of cost allocation workbooks, we found that the department allocated costs to the Adult Protective Services (APS) group incorrectly when using Tables 1 and 4.[21] In some instances, a portion of costs allocated to an activity via a cost allocation table must be reallocated using another cost allocation table. For example, if Table 1 includes a row that charges 10% of

[21] Table 1 is used to allocate indirect costs that benefit all programs administered by the department. Table 4 is used to allocate direct costs associated with the Office of General Counsel field staff.

Table 1 costs to APS, and the APS table includes a row that charges 60% to SSBG, then $1,000 charged to Table 1 will ultimately result in charging $60 to SSBG ($1,000 x 10% x 60%).

When fiscal staff allocated costs using Tables 1 and 4, which both included a row for APS, fiscal staff allocated all APS costs to the Social Services Block Grant (SSBG), instead of reallocating the costs to both SSBG and the Medical Assistance Program (Medicaid) using the appropriate cost allocation table.[22] This problem occurred throughout the audit period, July 1, 2016, through June 30, 2017. After we brought this matter to the attention of fiscal management, management addressed the matter promptly by recalculating allocation results for the division and entering a correcting journal entry in the department's accounting records to resolve the error.

Because the department's controls were not sufficient to identify and correct the error and because management did not correct the error until after the audit period, we questioned costs related to the overcharges to SSBG and undercharges to Medicaid. In total, SSBG was overcharged by $536,406, and Medicaid was undercharged by the same amount. The questioned costs are included in **Table 2** below.

Adult Protective Services – Non-salary Expenses

Based on our review of cost allocation workbooks fiscal staff used to allocate costs for the APS division, we found that fiscal staff allocated all APS non-salary expenses for August 2016 and September 2016 to SSBG instead of allocating the costs to both SSBG and Medicaid based on the results of random moment sampling, as required by the plan. We noted that an error within the cost allocation spreadsheets for these two months caused all expenses to be charged to SSBG, rather than to both programs.

Because the department's controls were not sufficient to identify and correct the error, we questioned costs related to the overcharges to SSBG and undercharges to Medicaid. In total, the SSBG program was overcharged by $54,510 of federal expenses, and Medicaid was undercharged by the same amount. The questioned costs are included in **Table 2** below.

Table 2
Combined Questioned Costs for Condition B

Program	Federal Expenditures	State Expenditures	Total Expenditures
Amount Overcharged			
Child Care and Development Block Grant	$ 13,492	$ -	$ 13,492
Social Services Block Grant	590,916	-	590,916
Total	**$604,408**	**$ -**	**$604,408**
Amount Undercharged			
Medical Assistance Program (Medicaid)	$(295,458)	$(295,458)	$(590,916)

[22] Although requested, fiscal staff did not provide us any program-specific regulations for Medicaid that indicated that these costs were prohibited from being charged to Medicaid.

State Administrative Expenses for Child Nutrition	(13,492)	-	(13,492)
Total	**$(308,950)**	**$(295,458)**	**$(604,408)**

Cause for Condition B

These errors were the result of errors in fiscal staff's cost allocation spreadsheets. Fiscal staff corrected the error related to the Appeals and Hearings division, as well as the error related to APS costs charged solely to SSBG on December 12, 2017. As of the end of our fieldwork, fiscal staff had not corrected the error related to APS' non-salary expenses.

Condition C. Fiscal Staff Used Incorrect Cost Allocation Tables to Allocate Costs for One Area

Based on our testwork, fiscal staff did not use the correct cost allocation table to allocate costs for the Family Assistance Renewal Processing unit. Fiscal staff's practice was to allocate costs for the unit (which primarily performs eligibility processing for the Supplemental Nutrition Assistance Program, Temporary Assistance for Needy Families Program, and the Medicaid program) using Table FA1-1. In accordance with the department's cost allocation plan, fiscal staff created this table using random moment sampling data. Family Assistance Service Centers, in contrast with eligibility renewal processing units, answer calls and emails pertaining to issues related to the above federal programs and other programs, and the cost allocation plan requires fiscal staff to allocate expenses related to service centers using Table FA-5M. Based on discussion with fiscal staff, department management converted a service center to a renewal processing unit in October 2014. The fiscal staff responsible for creating the cost allocation tables began to include the new renewal processing unit in the random moment time sampling procedures used to prepare FA1-1 cost allocation tables, as appropriate. However, the fiscal staff responsible for allocating costs based on cost allocation tables continued to use Table FA-5M instead of Table FA1-1 to allocate costs for the renewal processing unit for the period of July 1, 2016, through March 31, 2017. For the period of April 1, 2017, through June 30, 2017, fiscal staff began using Table FA1-1 to allocate these costs, as required by the cost allocation plan effective April 1. We questioned the differences caused by the use of Table FA-5M rather than Table FA1-1. See **Table 3** below.

Table 3
Questioned Costs for Condition C

Program	Federal Expenditures	State Expenditures	Total Expenditures
Amount Overcharged			
Child Support Enforcement	$455	$235	$690
Medical Assistance Program (Medicaid)	19,730	19,730	39,460
Social Services Block Grant	531	-	531
Vocational Rehabilitation	7	2	9
Total	**$20,723**	**$19,967**	**$40,690**
Amount Undercharged			
Child Care and Development Block Grant	$ -	$(1,061)	$(1,061)

Supplemental Nutrition Assistance Program	(13,988)	(13,988)	(27,976)
Temporary Assistance for Needy Families	(2,913)	(8,740)	(11,653)
Totals	**$(16,901)**	**$(23,789)**	**$(40,690)**

Cause for Condition C

Although fiscal staff updated the procedures used to create Tables FA-5M and FA1-1 following the conversion of a service center to a renewal processing unit in October 2014, the procedures used to allocate costs based on these tables were not updated until the amended cost allocation plan became effective on April 1, 2017.

Condition D: Risk Assessment

Given the problems identified during our fieldwork, we also reviewed the department's November 2016 Financial Integrity Act Risk Assessment and determined that top management assessed the risk that "Costs charged to a federal program are not allowable under program regulations" as having a remote likelihood and small impact; however, management did not identify any mitigating controls related to the issue. Given the unallowable costs and cost principles issues identified in this finding and in others during the current audit, such as 2017-015, 2017-033, and 2017-037, we concluded that management should have assessed the likelihood as reasonably possible, assessed the impact as large, and included a control activity to mitigate the risk in the department's annual risk assessment.

Criteria for Conditions A Through C

Title 45, *Code of Federal Regulations* (CFR), Part 95, Section 517(a), states, "A State must claim FFP [federal financial participation] for costs associated with a program only in accordance with its approved cost allocation plan." This requirement effectively extends to all programs administered by state public assistance agencies by Section C, Appendix VI, of 2 CFR 200 (formerly Section C of OMB A-87, Attachment D), which states,

> State public assistance agencies will develop, document and implement, and the Federal Government will review, negotiate, and approve, public assistance cost allocation plans in accordance with Subpart E of 45 CFR Part 95. The plan will include all programs administered by the state public assistance agency.

2 CFR 200.405(d) states,

> Direct cost allocation principles. If a cost benefits two or more projects or activities in proportions that can be determined without undue effort or cost, the cost must be allocated to the projects based on the proportional benefit. If a cost benefits two or more projects or activities in proportions that cannot be determined because of the interrelationship of the work involved, then . . . the costs may be allocated or transferred to benefitted projects on any reasonable documented basis.

45 CFR 95.509(a) states that the State shall promptly amend the cost allocation plan and submit the amended plan for approval if any of the following events occur:

> (1) The procedures shown in the existing cost allocation plan become outdated because of organizational changes, changes in Federal law or regulations, or significant changes in program levels, affecting the validity of the approved cost allocation procedures.
>
> (2) A material defect is discovered in the cost allocation plan by the Director, DCA [U.S. Department of Health and Human Services' Division of Cost Allocation] or the State.
>
> (3) The State plan for public assistance programs is amended so as to affect the allocation of costs.
>
> (4) Other changes occur which make the allocation basis or procedures in the approval cost allocation plan invalid.

45 CFR 95.519 states that if costs under a public assistance program are not claimed in accordance with the approved cost allocation plan or if the State failed to submit an amended cost allocation plan as required by Section 95.509, the costs improperly claimed will be disallowed.

Effect for All Conditions

Failure to allocate costs in accordance with the cost allocation plan and federal requirements increases the risk that fiscal staff will not assign an appropriate share of costs to programs and that federal grantors will disallow costs charged to federal programs.

Additionally, federal regulations address actions that federal agencies may impose in cases of noncompliance. As noted in 2 CFR 200.338, "If a non-Federal entity fails to comply with Federal statutes, regulations or the terms and conditions of a Federal award, the Federal awarding agency or pass-through entity may impose additional conditions," including, as described in Section 200.207, "Specific conditions":

> (1) Requiring payments as reimbursements rather than advance payments;
>
> (2) Withholding authority to proceed to the next phase until receipt of evidence of acceptable performance within a given period of performance;
>
> (3) Requiring additional, more detailed financial reports;
>
> (4) Requiring additional project monitoring;
>
> (5) Requiring the non-Federal entity to obtain technical or management assistance; or
>
> (6) Establishing additional prior approvals.

Furthermore, Section 200.338 also states,

> If the Federal awarding agency or pass-through entity determines that noncompliance cannot be remedied by imposing additional conditions [as

described above], the Federal awarding agency or pass-through entity may take one or more of the following actions, as appropriate in the circumstances:

(a) Temporarily withhold cash payments pending correction of the deficiency by the non-Federal entity or more severe enforcement action by the Federal awarding agency or pass-through entity.

(b) Disallow (that is, deny both use of funds and any applicable matching credit for) all or part of the cost of the activity or action not in compliance.

(c) Wholly or partly suspend or terminate the Federal award.

(d) Initiate suspension or debarment proceedings as authorized under 2 CFR part 180 and Federal awarding agency regulations (or in the case of a pass-through entity, recommend such a proceeding be initiated by a Federal awarding agency).

(e) Withhold further Federal awards for the project or program.

(f) Take other remedies that may be legally available.

Questioned Costs

We questioned a total of $2,131,602 due to the net amount of overcharges to federal programs, consisting of federal questioned costs of $1,540,999 and $590,603 in questioned costs related to state matching funds. See **Table 4** for details regarding all overcharges and undercharges.

Table 4
Combined Questioned Costs for All Conditions

Program	Federal Expenditures	State Expenditures	Total Expenditures
Amount Overcharged			
Child and Adult Care Food Program	$ 4,765	$ -	$ 4,765
Child Care and Development Block Grant	13,492	111,348	124,840
Child Support Enforcement	232,500	119,773	352,273
Community Services Block Grant	11,545	-	11,545
Independent Living Services for Older Individuals Who Are Blind	4,269	474	4,743
Social Security Disability Insurance	38,221	-	38,221
Social Services Block Grant	769,949	-	769,949
State Administrative Expenses for Child Nutrition	22,496	-	22,496
Supplemental Nutrition Assistance Program	269,989	269,989	539,978
Temporary Assistance for Needy Families	66,186	60,359	126,545
Vocational Rehabilitation	107,587	28,660	136,247
State Only Activities	-	-	-
Total	**$1,540,999**	**$590,603**	**$2,131,602**

Amount Undercharged			
Medical Assistance Program	$(327,943)	$(327,943)	$(655,886)
Total	**$(327,943)**	**$(327,943)**	**$(655,886)**

As noted above in Condition B, $549,898 of the questioned costs related to Condition B were resolved after the audit period; therefore, fiscal staff corrected the errors that led to $549,898 of the questioned costs in **Table 4** above.

This finding, in conjunction with findings 2017-012, 2017-013, 2017-015, 2017-018, 2017-037, and 2017-040, results in total known federal questioned costs exceeding $25,000 for a federal program which is audited as a major program. This finding, in conjunction with findings 2017-010, 2017-012, and 2017-015, results in total known federal questioned costs exceeding $25,000 for a federal program which is not audited as a major program.

Concerning questioned costs, 2 CFR 200.516(a)(3) requires us to report known questioned costs that are greater than $25,000 for a type of compliance requirement for a major program. Additionally, 2 CFR 200.516(a)(4) requires us to report known questioned costs that are greater than $25,000 for a federal program which is not audited as a major program.

According to 2 CFR 200.84,

> *Questioned cost* means a cost that is questioned by the auditor because of an audit finding:
>
> (a) Which resulted from a violation or possible violation of a statute, regulation, or the terms and conditions of a Federal award, including for funds used to match Federal funds;
>
> (b) Where the costs, at the time of the audit, are not supported by adequate documentation; or
>
> (c) Where the costs incurred appear unreasonable and do not reflect the actions a prudent person would take in the circumstances.

Recommendation

The Department Controller should ensure that the Department of Human Services' cost allocation plan is appropriately applied and that calculations in cost allocation spreadsheets are accurate.

The Commissioner of the Department of Human Services should assess all significant risks with sufficient attention to the impact and likelihood of the risk. The risk assessment and the mitigating controls should be adequately documented and approved by the Commissioner, who should implement effective controls to ensure compliance with applicable requirements; assign employees to be responsible for ongoing monitoring of the risks and any mitigating controls; and take action if deficiencies occur.

Management's Comment

Condition A. Fiscal Staff Prepared Three Cost Allocation Tables Incorrectly

We concur in part.

The department concurs that the cost allocation tables for CR-1 and 9A-2 were not prepared in accordance with the cost allocation plan in effect for July 1, 2016, through March 31, 2017. As noted in management's response from prior audit finding 2016-015, the approach utilized resulted in a more equitable distribution of costs than would have occurred had the tables been prepared as described in the previous plan; therefore, the department does not concur with the associated questioned costs. The methodologies utilized for preparation of CR-1 and 9A-2 were incorporated into the approved cost allocation plan that became effective on April 1, 2017. In regards to table ACS-3, a journal entry to correct the error noted will be completed by April 30, 2018.

Condition B. Fiscal Staff Did Not Detect Errors in Cost Allocation Workbooks for Four Areas

We concur.

Errors in cost allocation spreadsheets were not detected and corrected in a timely manner. Fiscal services reorganized into functional areas on October 1, 2017. As part of the reorganization, the cost allocation unit has been staffed with five (5) individuals whose sole responsibility is to oversee the department's cost allocation functions. Additional staff will provide more layers of review to detect and correct any errors in allocation spreadsheets. Two (2) of the three (3) errors noted in the finding have already been corrected. A journal entry to correct the 3^{rd} error noted will be completed by March 31, 2018.

Condition C. Fiscal Staff Used Incorrect Cost Allocation Tables to Allocate Costs for One Area

We concur.

Fiscal staff utilized the wrong table to allocate costs for one area. Errors related to first quarter were corrected on February 14, 2017. Errors related to the 2^{nd} and 3^{rd} quarter will be corrected by March 31, 2018.

Condition D. Risk Assessment

The department completes its annual risk assessment as required under *Tennessee Code Annotated*, Section 9-18-101 using guidance provided by the Tennessee Department of Finance and Administration (F&A). For the Department's November 2016 Financial Integrity Act Risk Assessment, risks of non-compliance were assessed by compliance type requirement for the Department as a whole. For the December 2017 Financial Integrity Act Risk Assessment, based on revised F&A guidance, risks were assessed on a more programmatic/divisional level.

Auditor's Comment

Condition A. Fiscal Staff Prepared Three Cost Allocation Tables Incorrectly

In management's comment, management states that "the approach utilized resulted in a more equitable distribution of costs than would have occurred had the tables been prepared as described in the previous plan."

Because management did not compile the allocation data needed to allocate costs based on square footage and device counts (or if they compiled it, they did not provide the new data to us), it is not clear how management concluded that adhering to the approved cost allocation plan in effect from July 1, 2016, through March 31, 2017, would have resulted in less equitable allocations. Management was required to obtain the necessary data and allocate costs based on square footage and device counts for this time period, and no evidence was provided that indicated that doing so would have resulted in less equitable allocations.

Finding Number	2017-015
CFDA Number	10.558, 10.559, 10.560, 10.561, 84.126, 84.177, 93.464, 93.558, 93.563, 93.569, 93.667, 93.747, 93,778, and 96.001
Program Name	Child and Adult Care Food Program Child Nutrition Cluster State Administrative Expenses for Child Nutrition Supplemental Nutrition Assistance Program Cluster Rehabilitation Services - Vocational Rehabilitation Grants to States Rehabilitation Services - Independent Living Services for Older Individuals Who are Blind ACL Assistive Technology Temporary Assistance for Needy Families Cluster Child Support Enforcement Community Services Block Grant Social Services Block Grant Elder Abuse Prevention Interventions Program Medicaid Cluster Disability Insurance/Supplemental Security Income Cluster
Federal Agency	Department of Agriculture Department of Education Department of Health and Human Services Social Security Administration
State Agency	Department of Human Services
Federal Award Identification Number	201616N109945, 201717N109945, 201616N253345, 201717N253345, 201616IS251445, 201717IS251445, 8044 H126A160063, 8044 H126A170063, H177B160064, H177B170064, 1601TNSGAT, 1701TNSGAT, G1502TNTANF, G1602TNTANF, 1604TNCSES, 1704TNCSES, G15B1TNCOSR, G16B1TNCOSR, G1501TNSOSR, G1601TNSOSR, 90EJSG001001, 05-1505TN5ADM, 05-1605TN5ADM, 05-1705TN5ADM, and 8826 04-17-04TNDI00
Federal Award Year	2015 through 2017
Finding Type	Significant Deficiency (10.558, 10.559, 10.561, 84.126, 93.558, 93.563, and 93.778) Noncompliance
Compliance Requirement	Allowable Costs/Cost Principles
Repeat Finding	2016-016
Pass-Through Entity	N/A
Questioned Costs	

CFDA	Federal Award Identification Number	Amount
10.558	201616N109945	$5,054
10.559	201717N109945	$674
10.560	201616N253345	$574
10.560	201717N253345	$5,798
10.561	201616IS251445	$38,507

10.561	201717IS251445	$19,380
84.126	8044 H126A160063	$2,010
84.126	8044 H126A170063	$926
84.177	H177B160064	$155
84.177	H177B170064	$2,829
93.464	1601TNSGAT	$6
93.464	1701TNSGAT	$83
93.558	G1502TNTANF	$2,469
93.558	G1602TNTANF	$9,662
93.563	1604TNCSES	$12,629
93.563	1704TNCSES	$72,804
93.569	G15B1TNCOSR	$7
93.569	G16B1TNCOSR	$70
93.667	G1501TNSOSR	$15,274
93.667	G1601TNSOSR	$20,876
93.747	90EJSG001001	$460
93.778	05-1505TN5ADM	$574
93.778	05-1605TN5ADM	$442
93.778	05-1705TN5ADM	$5,087
96.001	8826 04-17-04TNDI00	$892

As noted in the prior two audits, fiscal staff for the Department of Human Services did not ensure that personnel costs charged to federal grants were supported by adequate documentation, resulting in federal questioned costs of $217,242

Background

Federal regulations require the state to submit a cost allocation plan that outlines the procedures used to identify, measure, and allocate all costs to all programs the Department of Human Services (DHS) administers. The Department of Finance and Administration (F&A) creates, submits, and implements the cost allocation plan on DHS' behalf. DHS had two cost allocations plans that were effective during the audit period, July 1, 2016, through June 30, 2017. The first cost allocation plan was effective starting July 1, 2014, and was in effect until April 1, 2017, when the second cost allocation plan became effective.

F&A's method for allocating personnel costs to federal and state programs varies depending on whether the approved cost allocation plan identifies personnel costs as direct or indirect costs. Direct costs are costs that can be identified specifically with a particular final cost objective (a cost objective is a function, organizational subdivision, contract, grant, or other activity for which cost data are needed and for which costs are incurred). Indirect costs are costs that are incurred for a common or joint purpose benefiting more than one cost objective and that cannot be directly assigned to any specific federal or state programs without undue effort. Generally, the amount of resources needed to be expended to directly assign these indirect costs would be greater than any benefit that would be gained by assigning these costs.

Federal Documentation Requirements

Federal grant awards are subject to "Uniform Administrative Guidance," Title 2, *Code of Federal Regulations* (CFR), Part 200. Specifically, "Compensation – Personnel Services," 2 CFR 200.430, establishes standards for documenting employee time and effort when personnel expenditures are charged to federal awards. Charges to federal awards for salaries and wages must be based on records that accurately reflect the work performed and that are incorporated into the state's official records. Most importantly, the records must be supported by a system of internal control that provides reasonable assurance that the charges are accurate, allowable, and properly allocated; encompass both federally assisted and all other activities compensated by the state on an integrated basis; reflect the total activity for which the employee is compensated; and comply with the state's established accounting policies and practices.

Federal documentation guidelines permit the state to document employee time and effort using either physical or electronic records, such as recording information in online timekeeping systems and electronic spreadsheet documents. Regardless of the medium used, the documentation must identify the activities the employee worked on (such as federal or state programs) and the amount of time the employee worked on each activity.

While most of the federal programs DHS administers were subject to the Uniform Administrative Guidance during the audit period, the Child Care and Development Fund (CCDF) was not. For this federal program, the federal grantor has not established specific federal documentation requirements for personnel costs. Instead, federal regulations require CCDF's fiscal control and accounting procedures to be sufficient to permit the tracing of funds (in this case funds used for personnel costs) to a level of expenditure adequate to establish that such funds have not been used in violation of program requirements.

Payroll Procedures

Generally, all staff working in a division of DHS have their payroll costs allocated to one or more federal or state programs using the same methodology. For these employees, fiscal staff can allocate costs for all employees in the division at once, rather than track specific individuals' job assignments and charge programs accordingly.

In contrast, for employees who work on a temporary assignment in another division or who have recently moved from one division to another, fiscal staff perform a process to remove the employees' payroll costs from the employees' original divisions and reallocate the costs to the correct divisions. Specifically, fiscal staff periodically send out employee lists to division managers asking them to identify any staff assignment changes for their division. If the managers note any changes, fiscal staff include the applicable employee in the personnel exceptions list. Each quarter, fiscal staff reallocate payroll costs for employees on the personnel exceptions list to the appropriate federal or state programs.

For the personnel exceptions process to work effectively, it is critical that the employee list sent to each division manager is either based on or reconciled to a list of the employees whose payroll costs are actually charged to the manager's division. For example, the employee list sent to a division manager may correctly indicate that an individual is working on the Vocational

Rehabilitation program, but the accounting system may improperly charge the employee's time to a different federal program. Unless the information in the payroll records and the employee lists is reconciled, fiscal staff cannot detect and correct errors such as this, which would result in improper payroll charges.

Audit Procedures

To determine whether personnel costs were adequately supported and whether fiscal control procedures for personnel costs were sufficient, we selected a sample of 80 personnel cost expenditures, totaling $10,768, from the population of 2,400,636 personnel cost transactions, totaling $168,739,446, incurred during the audit period and charged to the federal programs listed in **Table 1**.

Table 1
Personnel Expenditures for Major Programs Under Audit

Program	Total Transactions Count	Total Expenditures
Child and Adult Care Food Program	2,709	$ 683,685
Child Care and Development Fund	346,304	16,847,938
Child Support Enforcement	159,763	10,339,984
Summer Food Service Program for Children	3,353	119,782
Supplemental Nutrition Assistance Program	828,049	97,594,232
Temporary Assistance for Needy Families	791,572	20,659,732
Vocational Rehabilitation Grants to States	268,886	22,494,093
Grand Total	**2,400,636**	**$168,739,446**

Source: Summarized using information from Edison, the state's accounting system.

In the prior audit, we found that management did not ensure personnel costs were supported by adequate documentation, and we found that fiscal control procedures for CCDF were insufficient. We also found that Child Support Enforcement (CSE) funds were used for unallowable activities. Management concurred in part with the prior-year finding and stated,

> The Department is currently in the process of revising the cost allocation plan. The Department expects to submit its first revision to the plan prior to April 1, 2017. In conjunction with the revision of the plan, labor distribution functionality in the general ledger (Edison) will be utilized to provide the ability for employees to report time spent on multiple federal programs within the system rather than using excel timesheets.

In this year's audit, we found that F&A's fiscal staff implemented the corrective actions identified above, which resulted in fewer errors. Although there was an overall reduction in errors, we found that fiscal staff still did not have adequate documentation to support payroll costs charged to federal awards (including errors related to the implementation of the electronic time reporting system). We also found that CSE funds were again used for unallowable activities.

Summary of Conditions

Based on our testwork, we found that the F&A Department Controller did not ensure that charges to federal awards were based on adequate supporting documentation (see Condition A) and did not ensure that charges to the CSE program were for allowable activities (see Condition B), resulting in total questioned costs of $348,044. Federal questioned costs were $217,242; the remaining $130,802 were state matching funds.

Condition A. Personnel Costs Were Not Supported by Adequate Documentation

Original Testwork

Based on our sample testwork, F&A's Department Controller did not ensure that personnel costs charged to federal awards were supported by adequate documentation for 2 of 80 personnel cost expenditures tested (2.5%). The issues were due to charging payroll amounts for an employee to the incorrect department ID[23] in Edison and charging leave costs improperly for an employee on the personnel exceptions list.

Regarding the employee's payroll charged to the incorrect department ID, we anticipated that the personnel exception process would have detected and corrected this issue if the process was designed properly and operating effectively. Upon further review of the personnel exception process, we determined that the control was not designed properly. Specifically, the list of employees sent to division managers for confirmations of employees' assignments was based on a human resources staffing query, rather than a list of employees whose payroll costs were charged to the manager's division. In addition, fiscal staff had not established a process to reconcile an employee list per the payroll data to the list of employees based on human resources data. We used data analysis procedures to reconcile the two data sources and identify an additional $344,995 in payroll costs charged to the incorrect department ID. See the Expanded Testwork section below.

Regarding improper leave charges, based on our discussion with fiscal staff and our review of records for employees whose time was supported by timesheets, we determined that fiscal staff charged all holiday and leave time to one federal program rather than allocating holiday and leave time across all federal and state programs the employees worked on. Generally, fiscal staff charged each employee's holiday or leave to the employee's main program assignment, even though the monthly timesheet indicated that the employee worked on other federal programs during the month. Specifically, we concluded that all non-working hours were generally charged to the individual's primary work assignment rather than allocated to other federal or state programs. For example, if an employee took two weeks of paid vacation leave, worked one week on CSE and one week on the Temporary Assistance for Needy Families (TANF) program, and CSE was the individual's primary work assignment, fiscal staff would charge three weeks of personnel costs (including all of the paid leave) to CSE and one week of personnel costs to TANF. Based on discussion with fiscal staff, this was fiscal staff's regular accounting practice until staff changed to the new Edison timesheet system beginning in April 2017.

[23] A department ID in Edison, the state's accounting system, is a way to assign expenditures to certain areas or divisions of the department. The department also uses department IDs to determine which methodology or cost allocation table should be used to allocate a cost among the federal programs.

2 CFR 200.431(b) states that leave is "allowable if all of the following criteria are met: . . . The costs are equitably allocated to all related activities, including Federal awards." We concluded that allocating all leave costs to only one benefitting program when an employee works on multiple programs does not result in a reasonable or equitable allocation of leave costs.

Expanded Testwork

As a result of the errors noted in the original sample testwork related to the personnel exceptions list, we expanded our work to identify additional employees that were charged to the incorrect department ID and to test a sample of payroll costs charged through the personnel exceptions process. In addition, to follow up on the prior audit finding, we reviewed direct personnel costs that were charged to more than one federal award and reviewed fiscal staff's implementation of the electronic timesheet process established to address prior audit findings.

Testwork for Payroll Costs Charged to the Incorrect Department ID

Because our original testwork suggested that the personnel exceptions process was not identifying staff whose payroll costs were charged to the incorrect department ID (and thus employees' payroll costs were being charged to the incorrect federal and state programs), we performed a data analysis procedure to identify additional staff charged to the incorrect department ID.

Specifically, we were provided staffing query data (the same type of query information provided to division managers for staff assignment verifications) for January 1, 2017, through March 31, 2017. For each employee in the data, we compared the employee's department ID per the staffing query data to the employee's department ID per their payroll costs and identified a list of employees charged to the incorrect department ID by pay period.

We removed the employees from our list if the incorrect and the correct department IDs both charged costs to programs using the same methodology (and thus no program was overcharged due to the error). Finally, we compared our list to fiscal staff's personnel exceptions list for January 2017 through March 2017 and removed any employees from our list who fiscal staff had already identified.

Our testwork identified a total of 70 staff (including 1 identified during our original testwork) whose payroll costs were charged to the incorrect department ID during the period January 1, 2017, through March 31, 2017, and who were not detected by the payroll exceptions process. The total amount of payroll costs charged to the incorrect department ID for these 70 individuals was $344,995 during the period January 1, 2017, through March 31, 2017. While we could determine the total amount of payroll costs ultimately charged to various programs, we could not determine the amount of questioned costs for each applicable federal program, as the information needed to calculate the questioned costs associated with each affected program was based on each employee's unique circumstances and was not readily available.

Sample Testwork for Payroll Costs Charged Through the Personnel Exceptions Process

To determine whether personnel costs charged through the personnel exceptions process were adequately supported and whether fiscal control procedures for personnel costs were sufficient, we selected a random sample of 25 employees whose payroll costs were allocated through the personnel exceptions process and reviewed supporting documentation for their costs.

Based on our sample testwork, the F&A Department Controller did not ensure that personnel costs charged to federal awards through the payroll exceptions process were supported by adequate documentation for 20 of 25 employees tested (80%). The total amount of payroll costs charged through the personnel exception process during the period July 1, 2016, through June 30, 2017, as well as a summary of the errors identified in our testwork, are exhibited in **Table 2**.

Table 2
Summary Information of Personnel Exception Population and Sample by Program

Program Name	Population Total	Dollar Amount of Sample Items Tested	Dollar Amount of Errors	Error Rate
Assistive Technology	$ 27,740	$ 6	$ 6	100%
Child and Adult Care Food Program	361,615	5,054	5,054	100%
Child Care and Development Fund	289,865	3,242	2,748	85%
Child Support Enforcement	361,340	49,393	45,094	91%
Community Services Block Grant	52,893	16	14	88%
Elder Abuse Prevention Interventions Program	59,519	499	451	90%
Independent Living Services for Older Individuals Who are Blind	957,109	36,935	2,691	7%
Independent Living State Grants	38,572	1,461	*(499)	-34%
Medical Assistance Program	189,671	14,778	11,058	75%
Social Security Disability Insurance	120,696	1,608	892	55%
Social Services Block Grant	148,995	50,178	36,150	72%
State Administrative Expenses for Child Nutrition	197,400	10,673	6,184	58%
Summer Food Service Program for Children	54,680	29,300	674	2%
Supplemental Nutrition Assistance Program	1,983,059	83,760	70,374	84%
Temporary Assistance for Needy Families	470,188	24,237	23,727	98%
Vocational Rehabilitation Grants to States	1,013,522	7,061	3,731	53%
Totals	**$6,326,864**	**$318,201**	**$208,349**	

*This amount is negative due to the program being undercharged in error. We did not question any costs for this item.

The issues noted above were due to various problems, including

- not preparing and maintaining official records documenting employee activity, such as timesheets, certifications, or similar documentation;

- not ensuring that supporting documentation for personnel costs was supported by a system of internal control that provided reasonable assurance that the charges were accurate, allowable, and properly allocated, as required;
- charging costs to a single federal program even though the employees' timesheets indicated that they worked on multiple programs;
- charging costs to multiple federal programs without documentation demonstrating how much time employees spent on each activity;
- not reallocating employees' costs in accordance with the allocation percentages identified in the supporting documentation;
- using indirect cost allocation methodologies that were not approved in DHS' cost allocation plan; and
- calculating allocation percentages incorrectly.

Even though the sample errors for some programs noted in **Table 2** above are small dollar errors, when projected to the population and combined with additional known questioned costs described in this finding, as well as in Findings 2017-010, 2017-012, 2017-013, 2017-014, 2017-018, 2017-027, 2017-031, and 2017-040, the questioned costs for the errors far exceed $25,000 for each federal program identified in **Table 2**. 2 CFR 200.516(a)(3) requires us to report known questioned costs when likely questioned costs are greater than $25,000 for a type of compliance requirement for a major program. 2 CFR 200.516(a)(4) requires us to report known questioned costs that are greater than $25,000 for a federal program that is not audited as a major program.

Review of Direct Personnel Costs Charged to More Than One Federal Award

For one employee whose payroll was charged to TANF, the Medical Assistance Program, and the Supplemental Nutrition Assistance Program, we found that fiscal staff did not ensure that $53,713 in payroll costs related to the Family Assistance Disaster Relief division were supported by personnel activity reports, semi-annual certifications, or other documentation sufficient to support the distribution of personnel costs to federal programs. Instead of allocating these payroll costs to programs based on documentation supporting actual time and effort distributions, fiscal staff allocated these payroll costs based on random moment time sampling, which was not approved in DHS' cost allocation plan. We questioned costs related to this error. See **Table 3** below for more details.

Table 3
Payroll Costs Related to the Family Assistance Disaster Relief Division

Program	Federal Expenditures	State Expenditures	Total Expenditures
Medical Assistance Program	$ 574	$ 574	$ 1,148
Supplemental Nutrition Assistance Program	22,700	22,700	45,400
Temporary Assistance for Needy Families	1,791	5,374	7,165
Totals	**$25,065**	**$28,648**	**$53,713**

Review of Fiscal Staff's Implementation of the Electronic Timesheet Process

Beginning April 2017, in select areas of DHS, fiscal staff implemented a new process that involved employees using Edison, the state's accounting system, to submit electronic timesheets that include sufficient information to support a distribution of costs to various programs. In the prior-year finding, we reported that these timesheets lacked sufficient documentation to support a distribution of costs to multiple programs; however, based on our observations in the current audit, the timesheets now include sufficient information for the staff who transitioned to the new process.

We reviewed the divisions' allocation of charges to federal programs using the new process and noted that, in some cases, employees reported their leave hours as a federal program activity instead of a leave activity. As a result, fiscal staff did not allocate the employees' leave and holiday pay equitably to all federal programs the employee worked on for the applicable pay period. We calculated the correct leave allocations for all employees using Edison task profile timesheets and compared our calculations to the actual amounts fiscal staff allocated. We noted that, during the period April 1, 2017, through June 30, 2017, federal programs were overcharged $1,121 out of the $94,326 in leave costs charged to federal programs using the new process. We questioned the overcharges to federal programs. See **Table 4** below for a full list of the differences:

Table 4
Overcharges (Undercharges) by Federal Program Due to Leave Allocation Errors

Federal Program	**Federal Expenditures**	**State Matching Expenditures**	**Total Expenditures**
Amount Overcharged			
Assistive Technology	$ 83	$ -	$ 83
Community Services Block Grant	63	-	63
Elder Abuse Prevention Interventions Program	122	41	163
Independent Living Services for Older Individuals Who Are Blind	562	62	624
State Administrative Expenses for Child Nutrition	188	-	188
Total	**$1,018**	**$ 103**	**$ 1,121**
Amount Undercharged			
Independent Living State Grants	$(164)	$ (18)	$ (182)
Medical Assistance Program	(99)	(99)	(198)
Social Security Disability Insurance	(30)	-	(30)
Social Services Block Grant	(216)	-	(216)
Vocational Rehabilitation	(391)	(104)	(495)
Totals	**$(900)**	**$(221)**	**$(1,121)**

<u>Criteria</u>

According to "Uniform Administrative Guidance," 2 CFR 200.430(i)(1), charges to federal awards for salaries and wages must be based on records that accurately reflect the work performed, and these records must (1) be supported by a system of internal control which provides reasonable assurance that the charges are accurate, allowable, and properly allocated; and (2) be incorporated into the official records of the non-Federal entity.

Furthermore, 2 CFR 200.430(i)(1)(vii) also states that if an employee works on more than one federal award, charges to federal awards for salaries and wages must be based on records that support the distribution of the employee's salary or wages among specific activities or cost objectives.

Additionally, according to 2 CFR 200.431(b)(2), the cost of fringe benefits in the form of regular compensation paid to employees during periods of authorized absences, such as for annual leave, sick leave, holidays, and other similar benefits, is only allowable if the costs are equitably allocated to all related activities, including federal awards.

45 CFR 95.517(a) states, "A State must claim FFP [federal financial participation] for costs associated with a program only in accordance with its approved cost allocation plan." This requirement effectively extends to all programs administered by state public assistance agencies by Section C, Appendix VI, of 2 CFR 200, which states,

> State public assistance agencies will develop, document and implement, and the Federal Government will review, negotiate, and approve, public assistance cost allocation plans in accordance with Subpart E of 45 CFR Part 95. The plan will include all programs administered by the state public assistance agency.

CCDF is not subject to the cost principles in Subpart E of the Uniform Administrative Guidance. Instead, 45 CFR 98.67(c)(2) states that fiscal control and accounting procedures must be sufficient to permit the tracing of funds to a level of expenditure adequate to establish that such funds have not been used in violation of CCDF regulations.

Cause

Testwork for Payroll Costs Charged to the Incorrect Department ID

Based on our discussion with fiscal staff, fiscal staff were not aware that information in the staffing query and information in the payroll records needed to be reconciled.

Sample Testwork for Payroll Costs Charged Through the Personnel Exceptions Process

Regarding inadequate documentation related to the personnel exceptions process, we noted that this issue was primarily the result of a lack of standard documentation practices for the process and a reliance on informal spreadsheets. Based on our review of the documentation, fiscal staff appeared to be preparing these informal spreadsheets rather than ensuring that the appropriate staff within DHS—such as the relevant employees or their supervisors—provided the documentation needed to support the payroll charges.

Review of Direct Personnel Costs Charged to More Than One Federal Award

Regarding improper charges related to the Family Assistance Disaster Relief division, for the period of July 2016 to March 2017, fiscal staff continued allocating the payroll costs of employees in some areas based on predefined percentages or other incorrect bases. This issue was corrected as of April 1, 2017, when DHS implemented a new cost allocation plan.

Review of Fiscal Staff's Implementation of the Electronic Timesheet Process

Regarding incorrect charges for leave related to the new timesheet process, employees did not appear to be adequately trained to ensure they entered their leave correctly, and fiscal staff had not established a process for identifying and correcting these errors.

Questioned Costs

We questioned $161,571 in federal costs and $102,111 in state matching funds, for a total of $263,682 in questioned costs. See **Tables 2** through **4** above for total questioned costs by program.

Condition B. Child Support Enforcement Funds Were Used for Unallowable Activities

F&A's Department Controller did not ensure that charges to the CSE program were for allowable activities. Specifically, fiscal staff charged to the CSE program $84,350 in costs for general administrative training provided through the Office of Learning and Professional Development (OLPD). The training costs were allocated to various programs as indirect costs; however, general administrative training was not allowable under the CSE program.

Criteria

According to 45 CFR 304.23(d), federal financial participation for CSE is not available for

> Education and training programs and educational services for State and county employees and court personnel except direct cost of short-term training provided to IV-D agency staff in accordance with §§304.20(b)(2)(viii) [related to reasonable and essential short-term training associated with the state's program of voluntary paternity establishment services] and 304.21 [related to reasonable and essential short-term training of court and law enforcement staff assigned on a full- or part-time basis to support enforcement functions under certain cooperative agreements].

Cause

DHS' approved cost allocation plans indicated that CSE funds may not be used for general administrative training provided through OLPD; therefore, the fiscal staff responsible for preparing the cost allocation plans were aware of this compliance requirement for CSE. Although the revised cost allocation plan, effective April 1, 2017, stated that "OLPD costs allocable to Child Support will be paid for out of State funds rather than Title IV-D consistent with 45 CFR 304.23(d)," fiscal staff continued to allocate OLPD costs to the CSE program.

Questioned Costs

We questioned $55,671 of unallowable federal costs charged to the CSE program and $28,679 in state matching costs, for a total of $84,350.

Condition C. Risk Assessment

Given the problems identified during our fieldwork, we also reviewed DHS' November 2016 Financial Integrity Act Risk Assessment. We determined that management did not document the mitigating controls associated with the risk that costs charged to a federal program are not allowable under program regulations in the annual risk assessment. Management documented in the annual risk assessment that there was a small impact and a remote (low) likelihood that costs charged to a federal program are not allowable under program regulations. Given the impact and frequency with which we identified noncompliance with the allowable costs/cost principles requirements in the current and prior audits, we concluded that management should have assessed the impact as high and the likelihood as probable (high) and included a control activity to mitigate the risk in the annual risk assessment.

Effect

Condition A

Failure to create and maintain sufficient documentation, and failure to create or follow fiscal controls and accounting procedures for personnel costs charged to federal awards, increases the risk of noncompliance with federal requirements and the possibility that federal agencies will seek to recover disallowed and/or unsupported costs.

Condition B

Failure to ensure that charges to federal awards are for allowable activities increases the risk that fiscal staff will not comply with federal requirements and the possibility that federal agencies will seek to recover disallowed costs.

All Conditions

Additionally, federal regulations address actions that federal agencies may impose in cases of noncompliance. As noted in 2 CFR 200.338, "If a non-Federal entity fails to comply with Federal statutes, regulations or the terms and conditions of a Federal award, the Federal awarding agency or pass-through entity may impose additional conditions," including, as described in Section 200.207, "Specific conditions":

(1) Requiring payments as reimbursements rather than advance payments;

(2) Withholding authority to proceed to the next phase until receipt of evidence of acceptable performance within a given period of performance;

(3) Requiring additional, more detailed financial reports;

(4) Requiring additional project monitoring;

(5) Requiring the non-Federal entity to obtain technical or management assistance; or

(6) Establishing additional prior approvals.

Furthermore, Section 200.338 also states, If the Federal awarding agency or pass-through entity determines that noncompliance cannot be remedied by imposing additional conditions [as described above], the Federal awarding agency or pass-through entity may take one or more of the following actions, as appropriate in the circumstances:

(a) Temporarily withhold cash payments pending correction of the deficiency by the non-Federal entity or more severe enforcement action by the Federal awarding agency or pass-through entity.

(b) Disallow (that is, deny both use of funds and any applicable matching credit for) all or part of the cost of the activity or action not in compliance.

(c) Wholly or partly suspend or terminate the Federal award.

(d) Initiate suspension or debarment proceedings as authorized under 2 CFR part 180 and Federal awarding agency regulations (or in the case of a pass-through entity, recommend such a proceeding be initiated by a Federal awarding agency).

(e) Withhold further Federal awards for the project or program.

(f) Take other remedies that may be legally available.

Summary of All Questioned Costs and Other Required Reporting

All Questioned Costs

Condition	Federal Questioned Costs	State Questioned Costs	Total Questioned Costs
Personnel Costs Not Supported by Adequate Documentation (Condition A)	$161,571	$102,123*	$263,694*
CSE Funds Used for Unallowable Activities (Condition B)	$ 55,671	$ 28,679	$ 84,350
Totals	**$217,242**	**$130,802**	**$348,044**

*Includes amounts in the Other Required Reporting section below.

This finding, in conjunction with findings 2017-010, 2017-012, 2017-013, 2017-014, 2017-018, 2017-026, 2017-027, and 2017-029 (which also included federal questioned costs for the allowable costs/cost principles federal compliance requirement), results in total known federal questioned costs exceeding $25,000 for a type of compliance requirement for five major federal programs. 2 CFR 200.516(a)(3) requires us to report known questioned costs that are greater than $25,000 for a type of compliance requirement for a major program.

This finding, in conjunction with findings 2017-010, 2017-12, 2017-013, and 2017-014, results in total known federal questioned costs exceeding $25,000 for two federal programs that are not audited as major programs. 2 CFR 200.516(a)(4) requires us to report known questioned costs that are greater than $25,000 for a federal program that is not audited as a major program.

According to 2 CFR 200.84,

Questioned cost means a cost that is questioned by the auditor because of an audit finding:

(a) Which resulted from a violation or possible violation of a statute, regulation, or the terms and conditions of a Federal award, including for funds used to match Federal funds;

(b) Where the costs, at the time of the audit, are not supported by adequate documentation; or

(c) Where the costs incurred appear unreasonable and do not reflect the actions a prudent person would take in the circumstances.

Other Required Reporting

In order to fulfill our reporting responsibilities under 2 CFR 200.516, we are also required to include the following information in this finding.

See Table 5 below for a summary of the sample errors identified in the "Original Testwork" section above:

Table 5
Summary of Sample Testwork Errors

Program	Population Total	Dollar Amount of Sample Items Tested	Dollar Amount of Error in Sample	Error Rate in Sample
SNAP	$97,594,232	$4,787.54	$0.46	0.01%
TANF	$20,659,732	$1,679.30	$11.04	0.66%
Grand Total	**$118,253,964**	**$6,466.84**	**$11.50**	

Even though the sample errors noted in Table 5 above are small dollar errors, when projected to the population and combined with the additional known questioned costs described in this finding as well as Findings 2017-10, 2017-12, 2017-013, and 2017-014, the likely questioned costs for the errors far exceed $25,000 for each federal program identified in Table 2. 2 CFR 200.516(a)(3), requires us to report known questioned costs when likely questioned costs are greater than $25,000 for a type of compliance requirement for a major program.

Recommendation

F&A's Commissioner should ensure adequate documentation of personnel costs, such as periodic certifications and personnel activity reports, is maintained unless the cognizant federal agency approves a substitute method. The Commissioner should also ensure that staff do not use CSE funds for general training costs and correctly allocate costs based on appropriate supporting documentation.

DHS' Commissioner should assess all significant risks, with sufficient attention to the impact and likelihood of the risk. The risk assessment and the mitigating controls should be adequately documented and approved by the Commissioner, who should implement effective controls to ensure compliance with applicable requirements; assign employees to be responsible for ongoing monitoring of the risks and any mitigating controls; and take action if deficiencies occur.

Management's Comment

Condition A:

We concur in part.

Payroll Costs Charged to the Incorrect Department ID

Based on review of supporting documentation for the 2 errors out of 80 noted, the questioned costs pertaining to these items amounted to $11.50. While the projected amount would exceed $25,000 and result in a reportable condition, the expansion of testwork appears broad given that it was largely focused on the time period prior to management's corrective actions that took place on April 1, 2017. Based on review of support for the expanded testwork items, management found no issue with over half of them. For the remaining items, the underlying cause was due to the lack of a reconciliation process between staffing pattern information and payroll information. A process to reconcile these two items will be developed by June 30, 2018.

Payroll Costs Charged Through the Personnel Exceptions Process

Management does not agree with the underlying premise leading to many of the issues noted. Many of the individuals noted as issues were allocated as aggregate allocations of support staff time or other departmental allocation statistics and, therefore, would not require timesheets that identified separate activities. Two timesheets were prepared by employees; however, they failed to sign them. This problem has already been corrected since Edison timesheets require employee submission and supervisor approval. The remaining items noted were a result of an outdated cost allocation plan as well as the underutilization of labor distribution functionality in Edison. These items were addressed with the April 1, 2017, cost allocation plan and related Edison timesheet utilization.

Review of Direct Personnel Costs Charged to More Than One Federal Award

A timesheet is kept for all employees that work for the department. Prior to April 1, 2017, the Edison timesheet was only sufficient documentation for charging programs allocated using statistics outside of Edison or employees working on one federal program. Supporting documentation for employees working on multiple programs was maintained outside of Edison. Revisions to the Edison system that took effect on April 1, 2017, allow all employees to adequately report their time by program in Edison. In this instance, the employee was allocated by a table; therefore, documentation was sufficient to support their time allocation. Management agrees that the allocation was not in accordance with the 2014 plan. The April 1, 2017 plan aligned management's practices for allocating this time with the approved cost allocation plan.

Review of Fiscal Staff's Implementation of the Electronic Timesheet Process

The department agrees that staff charged an immaterial amount of leave time to the incorrect taskprofile IDs. While the errors appear to simply be a learning curve related to the new process implemented in April 2017, fiscal services has implemented additional controls during the first quarter of state fiscal year 2018. Department IDs that should not have leave recorded in them are reviewed prior to running the department's cost allocations. If any leave is detected in non-leave department IDs, the costs are moved to leave department IDs and then cost allocation is performed.

Condition B:

We do not concur.

Costs charged to child support were for training provided directly to child support employees. Management strongly believes that the administrative training conducted by the department is essential for child support employees to understand how to use state systems and follow state policies during the administration of their duties as child support employees, and is therefore an allowable activity. The approved April 1, 2017 cost allocation plan clearly states that "Costs related to time spent on general administrative training are allocated to all benefiting programs based on filled full and part-time positions (including overlapping appointments) at the end of the prior quarter."

Risk Assessment

The department completes its annual risk assessment as required under *Tennessee Code Annotated*, Section 9-18-101 using guidance provided by the Tennessee Department of Finance and Administration (F&A). For the Department's November 2016 Financial Integrity Act Risk Assessment, risks of non-compliance were assessed by compliance type requirement for the Department as a whole. For the December 2017 Financial Integrity Act Risk Assessment, based on revised F&A guidance, risks were assessed on a more programmatic/divisional level.

Auditor's Comment

Condition A. Personnel Costs Were Not Supported by Adequate Documentation

Payroll Costs Charged to the Incorrect Department ID

Management states that based on its "review of support for the expanded testwork items, management found no issue with over half of them." Management sent us an email indicating why it believed that many of the issues noted were not an issue; however, management's comments and inquiries in the email indicated that management had not reviewed all of the details provided. We requested that management review the details and then schedule a meeting with us to discuss the items management still believed were not problems, but management did not follow up with us to resolve the items in question.

Payroll Costs Charged Through the Personnel Exceptions Process

Management states, "Many of the individuals noted as issues were allocated as aggregate allocations of support staff time or other departmental allocation statistics and therefore, would not require timesheets that identified separate activities." These issues were not noted due to a lack of timesheets. Instead, we noted issues for these staff for a variety of reasons, including

1. the allocation methodologies were not in accordance with the department's cost allocation plan;
2. fiscal staff did not allocate costs in accordance with the allocation percentages identified in supporting documentation;
3. fiscal staff provided allocation statistics for divisions without evidence that the employees actually worked in those divisions; and
4. internal controls over payroll were inadequate, because employees' activities were documented on spreadsheets with no indication of who prepared them or when they were prepared.

Condition B. Child Support Enforcement Funds Were Used for Unallowable Activities

Although management states, "Costs charged to child support were for training provided directly to child support employees," the questioned costs were indirect costs charged to the Child Support Enforcement program and all other programs administered by the department. This distinction is important, because while direct costs are allowable in certain circumstances, indirect costs associated with training programs are not allowable.

Regarding management's comment that it "strongly believes that the administrative training . . . is essential for child support employees . . . and is therefore an allowable activity," we must use federal criteria to determine the allowability of a cost, not management's belief. As stated in 45 CFR 304.23(d), federal funding is not available for education and training programs and educational services except for the "**direct cost** [emphasis added] of short-term training provided to IV-D agency staff" related to specific program activities. Since the costs we questioned were indirect costs related to general administrative training, the costs were not allowable.

The federal government's approval of a cost allocation plan that is inconsistent with program-specific regulations does not authorize the state to waive said regulations.

Finding Number	2017-028
CFDA Number	84.126
Program Name	Rehabilitation Services - Vocational Rehabilitation Grants to States
Federal Agency	Department of Education
State Agency	Department of Human Services
Federal Award Identification Number	8044 H126A160063 and 8044 H126A170063
Federal Award Year	2016 and 2017
Finding Type	Significant Deficiency and Noncompliance
Compliance Requirement	Program Income
Repeat Finding	2016-017
Pass-Through Entity	N/A
Questioned Costs	N/A

As noted in the prior two audits, fiscal staff for the Department of Human Services requested additional federal funds before ensuring all program income and refunds had been spent

Background

The U.S. Department of Education provides Vocational Rehabilitation Grants to help states operate comprehensive Vocational Rehabilitation (VR) programs that help individuals with disabilities gain, maintain, or return to employment. In Tennessee, the Department of Human Services (DHS) administers VR through its Division of Rehabilitation Services. The Department of Finance and Administration (F&A) is responsible for adequate cash management for all of DHS.

As DHS incurs expenditures, F&A fiscal staff periodically request funds, called draw requests, from the federal grantors. Based on the nature of the federal award, meeting federal grant objectives can result in income generated as a direct result of the programs' operations. This generated income is known as program income.

In certain circumstances, DHS may recover funds it has previously spent from the grant. These recoveries of expenditures are identified as refunds to the program. Per Title 34, *Code of Federal Regulations* (CFR), Part 361, Section 63(c)(3)(ii), to the extent available, VR regulations require the state to spend program income and refunds before requesting additional federal funds. F&A generally does not record expenditures of program income in the accounting records to demonstrate that program income has been spent. Instead, F&A generally demonstrates that fiscal staff have spent program income and refunds by reducing the amount of federal funds requested.

For example, assume DHS receives $100 in program income and then spends $200 for services A and B. The accounting records would show $100 in federal funds expenditures for service A, $100 in federal funds expenditures for service B, and $100 in program income received as a credit against services A and B. In this example, F&A would bill the federal government $100 (service A (100) + service B (100) – program income received (100)). This accounting treatment demonstrates that F&A used the $100 in program income to fund $100 of services A and B; however, it is important to note that until the program income appears in the billing records as a credit reducing the amount of federal funds requested, there are no accounting records that demonstrate that the program income has been spent. As a result, if F&A requested $200 for services A and B in this example, we would conclude that F&A violated regulations requiring program income to be spent before requesting additional federal funds, because the accounting system would not identify a disbursement of the $100 in program income.

In the prior audit, we found that fiscal staff did not ensure that program income and refunds had been spent before requesting additional federal funds, and the Fiscal Directors and Accountants did not ensure that Child Support Enforcement (CSE) expenditures were net of all applicable credits[27] and program income.

Department management concurred with the prior-year finding and stated, "The Department revised the process for approving cash receipts in the cash receipting system (iNovah) in December 2015. Cash receipt batches are now approved daily" and "The Department has taken several corrective action steps since the errors occurred."

Based on our current testwork, we found that fiscal staff had ensured CSE expenditures were net of all applicable credits; however, we found that fiscal staff still did not ensure that program income and refunds had been spent before requesting federal funds.

Condition - Program Income and Refund Cash Receipts Were Not Disbursed Timely

We reviewed all 347 VR program income and refund cash receipts, totaling $3,176,639, that fiscal staff received and recorded in Edison revenue accounts during the period July 1, 2016, through June 30, 2017.

For each transaction, we identified

- the date the department received the program income or refund;
- the next federal funds request date after the program income or refund was received; and
- the date the program income or refund was spent.

We contacted the federal grantor, the Rehabilitation Services Administration (RSA) within the U.S. Department of Education, for additional guidance related to compliance with the requirement to spend program income and refunds before requesting additional federal funds. We explained fiscal staff's accounting process for program income and refunds, including reasonable delays between receiving and using program income that we believe are unavoidable in an environment with adequate internal controls. The RSA official noted, as an example, that he did not expect fiscal staff to delay requesting federal funds to meet payroll solely because fiscal staff received program income moments before planning to request the federal funds.

Based on this conversation, and after considering various factors related to the timing of processing program income and refunds, such as holidays, staff sick leave, and the average time it takes to

[27] Applicable credits refer to those receipts or reduction of expenditure type transactions that offset or reduce costs that are allocated to federal awards, including refunds and program income required to be used to reduce federal expenditures.

process transactions, we did not consider program income and refunds to be available per 34 CFR 361.63(c)(3)(ii) until one week after receipt. Therefore, we noted no problems unless program income and refunds had been on hand for at least a week and fiscal staff requested additional federal funds without first spending the program income or refund.

We noted that for 31 of the 347 receipts of program income and refunds tested (9%), totaling $55,023, F&A's Fiscal Directors and Accountants could not demonstrate that the program income and refunds had been spent before requesting additional federal funds. Per the accounting records, staff spent 25 receipts of program income and refunds, totaling $54,877, from 1 to 23 days (average of 6 days) after the next request of federal funds. The remaining 6 items, totaling $146, were still on hand and had not been spent by the end of the audit period, June 30, 2017. See **Table 1** below for more details.

Table 1
Vocational Rehabilitation Program Income Received

Days Late	Amount of Program Income	Number of Program Income Transactions
1	$17,439	12
8	11,582	9
14	6,406	2
17	14,289	1
23	5,161	1
Not Disbursed	146	6
Totals	**$55,023**	**31**

Risk Assessment

Given the problems identified during our fieldwork, we also reviewed DHS' November 2016 Financial Integrity Act Risk Assessment and determined that top management assessed the risk that program income is not spent before additional federal cash draws as having a remote likelihood and small impact; however, management did not identify any mitigating controls related to the issue and stated that controls are operating effectively. Given the frequency with which we noted that program income was not spent before fiscal staff made additional federal cash draws in this audit and in prior audits, we concluded that management should have assessed the likelihood as reasonably possible (medium).

Criteria

34 CFR 361.63(c)(3)(ii) states,

> Notwithstanding 2 CFR 200.305(a) and to the extent that program income funds are available, a State must disburse those funds (including repayments to a revolving fund), rebates, refunds, contract settlements, audit recoveries, and interest earned on such funds before requesting additional funds from the Department.

Cause

Based on discussion with the F&A Department Controller, this issue was primarily the result of decentralized accounting processes. Specifically, staff in one city were responsible for depositing program income; however, they did not perform the remaining accounting duties required to disburse the program income. Instead, the staff would mail (rather than fax or email) the documentation to fiscal staff in a nearby city, who would then perform the accounting duties required to disburse the program income. It appears that the delay inherent in these coordination activities, along with mail delivery times, may have caused most of the issues noted. The cause is not clear, however, because according to the Accountant and Fiscal Director, the Accountant did not rely on the mailed documentation to approve deposits in the financial management system during the audit period. Instead, the Accountant relied on the controls in place at the decentralized location and only performed a perfunctory review when approving deposits. According to the Department Controller, beginning in December 2017, the depositing and accounting functions are now centralized in one city, which should expedite disbursing VR program income in the future.

Effect

Failure to spend refunds and program income prior to requesting additional federal funds results in transfers of funds between the federal government and the state in violation of federal regulations. In addition, the state may earn interest (to which it is not entitled) on federal funds drawn prior to the appropriate offset of program income or refund expenditures. Additionally, federal regulations address actions that federal agencies may impose in cases of noncompliance. As noted in 2 CFR 200.338, "If a non-Federal entity fails to comply with Federal statutes, regulations or the terms and conditions of a Federal award, the Federal awarding agency or pass-through entity may impose additional conditions," including, as described in Section 200.207, "Specific conditions":

> (1) Requiring payments as reimbursements rather than advance payments;
>
> (2) Withholding authority to proceed to the next phase until receipt of evidence of acceptable performance within a given period of performance;
>
> (3) Requiring additional, more detailed financial reports;
>
> (4) Requiring additional project monitoring;
>
> (5) Requiring the non-Federal entity to obtain technical or management assistance; or
>
> (6) Establishing additional prior approvals.

Section 200.338 also states,

> If the Federal awarding agency or pass-through entity determines that noncompliance cannot be remedied by imposing additional conditions [as described above], the Federal awarding agency or pass-through entity may take one or more of the following actions, as appropriate in the circumstances:

(a) Temporarily withhold cash payments pending correction of the deficiency by the non-Federal entity or more severe enforcement action by the Federal awarding agency or pass-through entity.

(b) Disallow (that is, deny both use of funds and any applicable matching credit for) all or part of the cost of the activity or action not in compliance.

(c) Wholly or partly suspend or terminate the Federal award.

(d) Initiate suspension or debarment proceedings as authorized under 2 CFR part 180 and Federal awarding agency regulations (or in the case of a pass-through entity, recommend such a proceeding be initiated by a Federal awarding agency).

(e) Withhold further Federal awards for the project or program.

(f) Take other remedies that may be legally available.

Recommendation

The Commissioners of DHS and F&A should ensure that VR program income and refunds are spent prior to drawing additional federal funds. This should include verifying that staff deposit VR program income and refunds timely and identify receipts as VR program income and refunds in the accounting records timely. The Department Controller should ensure that fiscal staff take reasonable efforts to identify unidentified deposits timely and that staff document the nature and timing of these efforts.

The Commissioner of DHS should assess all significant risks, with sufficient attention to the impact and likelihood of the risk. The risk assessment and the mitigating controls should be adequately documented and approved by the Commissioner, who should implement effective controls to ensure compliance with applicable requirements; assign employees to be responsible for ongoing monitoring of the risks and any mitigating controls; and take action if deficiencies occur.

Management's Comment

We concur in part.

All of the items noted in the finding were items that were deposited when received in accordance with the Department of Finance and Administration's Policy 25; however, the transactions were not identified as program income until after they were deposited. It should be noted that 21 of the 31 transactions were a result of two deposits. Once identified with adequate support, they were immediately recorded as program income and the corresponding offset to federal expenditures was completed. The clearing account in which the funds were recorded upon deposit must be reconciled and certified on a monthly basis ensuring that unidentified deposits are resolved in a timely manner.

The department recognized that the decentralized business process resulting in these deposits originally being recorded as unidentified receipts had become outdated and, accordingly, on December 1, 2017, cash receipting was centralized.

Auditor's Comment

Based on review of the support received by DHS staff, the staff had indicated on the documentation (such as the receipts) that the transactions were program income at the time of deposit.

Finding Number	2017-029
CFDA Number	84.126
Program Name	Rehabilitation Services - Vocational Rehabilitation Grants to States
Federal Agency	Department of Education
State Agency	Department of Human Services
Federal Award Identification Number	8044 H126A160063 and 8044 H126A170063
Federal Award Year	2016 through 2017
Finding Type	Significant Deficiency – Matching, Level of Effort, Earmarking Material Weakness – Reporting Noncompliance
Compliance Requirement	Matching, Level of Effort, Earmarking Reporting
Repeat Finding	2016-039 2016-042
Pass-Through Entity	N/A
Questioned Costs	N/A

For the third year, fiscal staff for the Department of Human Services did not comply with financial reporting requirements for the Vocational Rehabilitation Grants to States program, and fiscal staff did not comply with maintenance of effort requirements

Background

The U.S. Department of Education's Rehabilitation Services Administration (RSA) provides Vocational Rehabilitation Grants to assist states in operating comprehensive vocational rehabilitation programs to help individuals with disabilities gain, maintain, or return to employment. In Tennessee, Vocational Rehabilitation is administered by the Department of Human Services (the department or DHS) through its Division of Rehabilitation Services. The Department of Finance and Administration (fiscal staff) is responsible for performing all fiscal-related duties on behalf of the department, including the submission of financial reports to RSA. As part of the grant's requirements, the state matches the federal funds by using state and other non-federal funds, such as funds from local governments and donations, to pay 21.3% of all Vocational Rehabilitation expenditures. Fiscal staff draw down federal Vocational Rehabilitation funds using the U.S. Department of Education's G5 grants management system.

The department is required to file a Federal Financial Report, the SF-425 report, semi-annually for each federal fiscal year's Vocational Rehabilitation grant. The semi-annual reporting periods are April 1 through September 30 and October 1 through March 31. Reports are generally due to RSA 45 days after the close of the reporting period.

Once it receives the SF-425 reports, RSA reviews the department's reports and makes the following determinations:

- whether the department is permitted to carry over Vocational Rehabilitation funds into the next federal fiscal year;

- if the department must return any unobligated federal program income to RSA; and
- if the department complied with various compliance requirements.

General Reporting Requirements

Obligations

RSA requires grantees (in this case, the department) to track and report the amounts and funding sources of obligations.[28] In addition, the department must track these obligations by obligation date and in terms of their status as unliquidated or liquidated.[29]

Program Income

In addition, RSA's instructions require the department to report the amount of program income expended in accordance with the federally prescribed addition alternative methodology. To ensure the expenditures of program income are included on the proper SF-425 report, the department must match expenditures of program income to the federal fiscal year (FFY) in which that program income was received. The process of matching the expenditures of program income to the year in which the income was received is necessary to record expenditures of program income on the correct SF-425 report.

RSA requires the department to complete a separate SF-425 report for each federal Vocational Rehabilitation grant award until each award's period of performance ends;[30] therefore, if the department carries over federal Vocational Rehabilitation funds into the subsequent federal fiscal year, the department must submit two SF-425 reports for each reporting period in the subsequent federal fiscal year.

During the 2015 single audit, we identified several critical deficiencies in the preparation of DHS' Vocational Rehabilitation SF-425 Federal Financial reports. Specifically, we found that department management did not ensure that the department's financial management systems were sufficient to permit the preparation of the SF-425 reports and that fiscal staff did not ensure that the reports were complete and accurate. In accordance with federal regulations, the department entered into a Corrective Action Plan with RSA during the prior audit period to correct the SF-425 reporting deficiencies. As part of the Corrective Action Plan, the department completed or revised SF-425 reports for the 2014-2017 grant awards during the current audit period.

To determine whether the department properly reported required financial information in its SF-425 reports during the current audit period, we tested the semi-annual SF-425 reports for the period ended September 30, 2016, for the FFY 2016 grant award and the report for the period ended

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[28] Obligations are the amounts of orders placed, contracts and subgrants awarded, goods and services received, and similar transactions during a given period that will require payment by the grantee during the same or a future period.
[29] For reports prepared on an accrued expenditure basis, federal regulations require obligations to be classified as unliquidated when the corresponding expenditure for the obligation has not yet been recorded.
[30] Period of performance means the time during which the non-federal entity may incur new obligations to carry out the work authorized under the federal award.

March 31, 2017, for the FFY 2017 grant award. During the current audit, we found that the department had made improvements to the reporting processes, including

- creating a reporting policy.
- correcting accounting records.
- modifying accounting systems to track required information, and
- improving review and control processes.

Despite these steps to resolve these matters during the current audit period, we found that department management still did not ensure that the required SF-425 reports were accurately prepared during the audit period, July 1, 2016, through June 30, 2017.

Condition

Portions of the SF-425 Reports Were Incomplete or Inaccurate

(A) The Accountant incorrectly calculated the federal share of expenditures for line 10e of both reports. Federal expenditures were overstated by $530,827 and $74,115 in the FFY 2016 and FFY 2017 reports, respectively, due to fiscal staff improperly including federal expenditures arising from obligations incurred in prior federal fiscal years. Per RSA's period of performance guidance, if a contract is signed in FFY 2015, for example, the expenditures associated with the contract should be reported on the FFY 2015 report, even if the services provided under the contract are performed in FFY 2016 and beyond.

The Accountant also improperly excluded pending expenditure adjustments totaling negative $95,934 from federal expenditures and instead reported these items as adjustments to federal unliquidated obligations. In addition, the Accountant improperly included a proposed adjusting journal entry that had not been recorded in the accounting records at the time the report was prepared that increased federal expenditures by $243,399. The accounting records did not indicate that this transaction occurred during the reporting period. For both reports, the Accountant also understated federal expenditures (and overstated program income expended) due to reducing federal expenditures for unexpended program income. Since the program income was on hand and had not yet been used to reduce federal funds requests at the end of the reporting period, the reported federal expenditures should not have been reduced by the amount of program income on hand.

Finally, in the September 30, 2016, report, we identified a duplicate transaction totaling $20,907 during our testwork procedures. This transaction was charged to the program twice, but a reversing entry corrected the error after the report was submitted.

Table 1
Federal Share of Expenditures Calculated Incorrectly

FFY of Grant Award	End of Reporting Period	Line	Line Description	Department Reported	State Audit Calculations	Difference
2016	9/30/2016	10e	Federal Share of Expenditures	$40,241,238	$39,364,747	$876,491
2017	3/31/2017	10e	Federal Share of Expenditures	$20,183,064	$20,103,259	$79,805

(B) The Accountant incorrectly calculated the federal share of unliquidated obligations for line 10f of both reports tested. For both reports, the Accountant relied on a Procurement Report extracted from the state's accounting system to determine the remaining amount of outstanding purchase orders. Based on that report, the Accountant improperly included a purchase order for a contract that is not associated with the Vocational Rehabilitation Grants to States (VR) program as well as two purchase orders that did not obligate 2016 grant award funds. In addition, while the reported numbers agreed with the Procurement Report data, the data did not always agree with the accounting records. The data was included in the calculation for line 10f in the amount of $5,791,025 for the September 30, 2016, report tested and $1,472,851 for the March 31, 2017, report tested. We requested an explanation of the difference from fiscal staff but did not receive a response. Because we could not determine the accurate amount to report, we prepared the State Audit Calculations below assuming that the procurement data was correct.

For the September 30, 2016, report tested, the Accountant also included an expenditure adjustment that was not booked until December of 2016, incorrectly estimated amounts of obligations, included at least $150,000 in duplicate obligations, and incorrectly included pending expenditure adjustments as obligations instead of expenditures.

In the 2016 report we tested, the Accountant included $281,679 in estimated unliquidated obligations; however, the Accountant did not include any estimated unliquidated obligations in the 2017 report. While the reporting instructions do not explicitly state whether estimates should be included, we concluded that, if performed consistently, it was reasonable to estimate the amounts of obligations associated with utilities and similar services where the department knows the service has been provided to the department as of the reporting date (and therefore constitutes a valid obligation), but the department is not aware of the amount of the obligation. We attempted to determine the potential estimate for unliquidated obligations for 2017 to ensure the Accountant was consistently reporting unliquidated obligations; however, we could not perform the calculations because the information was not readily available.

For the March 31, 2017, report tested, the Accountant improperly reduced the amount of unliquidated obligations reported by $297,872 in program income received after the end of the reporting period.

Table 2
Federal Share of Unliquidated Obligations Calculated Incorrectly

FFY of Grant Award	End of Reporting Period	Line	Line Description	Department Reported	State Audit Calculations	Difference
2016	9/30/2016	10f	Federal Share of Unliquidated Obligations	$6,145,906	$5,607,169	$538,737
2017	3/30/2017	10f	Federal Share of Unliquidated Obligations	$1,740,134	$2,038,006	($297,872)

(C) The Accountant incorrectly calculated the recipient share of expenditures for line 10j. Because these figures are calculated simultaneously as the federal share of expenditures and unliquidated obligations described in Sections A and B above, the reasons for the discrepancies in these figures are the same as described in Sections A and B.

Table 3
Recipient Share of Expenditures Calculated Incorrectly

FFY of Grant Award	End of Reporting Period	Line	Line Description	Department Reported	State Audit Calculations	Difference
2016	9/30/2016	10j	Recipient Share of Expenditures	$13,054,271	$12,742,808	$311,463
2017	3/30/2017	10j	Recipient Share of Expenditures	$5,730,568	$5,755,311	($24,743)

(D) The Accountant entered the incorrect dates in field 11c for Indirect Costs "Period From" and 11d for Indirect Costs "Period To." According to the report instructions, these fields should reference the period during which the approved Cost Allocation Plan is active, but the Accountant entered the reporting period instead.

Table 4
Dates for Indirect Costs Entered Incorrectly

FFY of Grant Award	End of Reporting Period	Line	Line Description	Department Reported	State Audit Calculations	Difference
2016	9/30/2016	11c	Indirect Costs "Period From"	October 1, 2015	July 1, 2014	N/A
2016	9/30/2016	11c	Indirect Costs "Period To"	September 30, 2016	Blank	N/A
2017	3/31/2017	11c	Indirect Costs "Period From"	October 1, 2016	July 1, 2014	N/A

(E) The Accountant calculated the Indirect Cost Base and Federal Share of Indirect Costs incorrectly for lines 10d and 10f on both reports tested. The department's reporting methodology involved reporting all grant transactions that were not classified to a particular department ID as indirect costs. This methodology inaccurately reports some direct costs as indirect costs and excludes some indirect costs.

Table 5
Indirect Cost Base and Federal Share of Indirect Costs Calculated Incorrectly

FFY of Grant Award	End of Reporting Period	Line	Line Description	Department Reported	State Audit Calculations	Difference
2016	9/30/2016	11d	Indirect Cost Base	$7,541,463	$6,087,802	$1,453,661
2016	9/30/2016	11f	Federal Share of Indirect Cost	$6,029,510	$4,885,505	$1,144,005
2017	3/31/2017	11d	Indirect Cost Base	$2,812,095	$2,537,753	$274,342
2017	3/31/2017	11f	Federal Share of Indirect Cost	$2,203,460	$1,987,549	$215,911

(F) The Accountant incorrectly reported program income received for line 10l of the FFY 2017 March 31, 2017, report. The Accountant incorrectly excluded one journal entry, resulting in an understatement of $28,544.

Table 6
Program Income Received Reported Incorrectly

FFY of Grant Award	End of Reporting Period	Line	Line Description	Department Reported	State Audit Calculations	Difference
2017	3/31/2017	10l	Total Federal Program Income Earned	$990,959	$1,019,503	($28,544)

(G) The Accountant incorrectly reported program income expended for line 10n on both reports. The FFY 2016 report overstated the amount of program income expended by the end of the reporting period by $14,575, and the FFY 2017 report understated the amount of program income expended by $5,691.

Table 7
Program Income Expended Reported Incorrectly

FFY of Grant Award	End of Reporting Period	Line	Line Description	Department Reported	State Audit Calculations	Difference
2016	9/30/2016	10n	Program Income Expended in Accordance with the Addition Alternative	$3,722,001	$3,707,426	$14,575
2017	3/31/2017	10n	Program Income Expended in Accordance with the Addition Alternative	$990,959	$996,650	($5,691)

(H) The Accountant incorrectly reported the recipient share of unliquidated obligations in line 12d on both reports. Because these figures were determined simultaneously with the federal share of unliquidated obligations reported on line 10f, the reasons for these discrepancies are the same as in section B above.

Table 8
Recipient Share of Unliquidated Obligations Reported Incorrectly

FFY of Grant Award	End of Reporting Period	Line	Line Description	Department Reported	State Audit Calculations	Difference
2016	9/30/2016	12d	Recipient Share of Unliquidated Obligations	$1,593,254	$1,464,050	$129,204
2017	3/30/2017	12d	Recipient Share of Unliquidated Obligations	$137,206	$161,949	($24,743)

(I) The Accountant incorrectly reported Federal Program Income Transferred to the Independent Living Services for Older Individuals who are Blind Program in line 12f of the 2016 report tested. The Accountant improperly included a journal to transfer those funds that had not occurred as of the report date.

Table 9
Federal Program Income Transferred Reported Incorrectly

FFY of Grant Award	End of Reporting Period	Line	Line Description	Department Reported	State Audit Calculations	Difference
2016	9/30/2016	12f	Federal Program Income Transferred to Independent Living Services for Older Individuals who are Blind Program	$1,225,378	$981,979	$243,399

Controls Over the Reporting Process Were Inadequate

During the performance of our testwork, we noted that the controls over the reporting process were inadequate to ensure that the department properly reported accurate information related to certain lines of the submitted SF-425 reports. Specifically, the Accountant referenced line 10n, Program income expended in accordance with the addition alternative, directly from line 10l, Total Federal program income earned, without any evidence that the department verified that the program income was actually expended at the end of the reporting period. Similarly, line 10e, Federal share of expenditures, was reduced by program income received instead of by the amount of program income used to reduce the federal draw. Likewise, some misstatements were related to allowable transfers that the department intended to make to other programs, but that had not been performed at the end of the reporting period. When reports are submitted, all financial activity included in the reports should be based on underlying accounting records that demonstrate that the activity occurred during the reporting period, rather than expectations about financial activity that may occur in the future. Additionally, the department did not have procedures in place to ensure that obligations and expenditures were only included in calculations once and not double-counted due to the items being included in multiple information sources.

Finally, we noted that the department's reporting methodology related to the construction of facilities for community rehabilitation program purposes (construction projects) was not adequate. A separate agency within the state, the State Building Commission, manages these projects and bills the Department of Human Services for the federal share of the projects. While fiscal staff included the federal share of expenditures for these projects in SF-425 reports, staff did not use the related underlying obligation dates to ensure the expenditures were reported on the correct grant year's report. In addition, the reporting process did not involve reviewing the State Building Commission's records to identify and accurately report other types of financial activity related to construction projects. As a result, financial activity related to construction projects was excluded from federal and non-federal unliquidated obligations and the non-federal share of expenditures for construction projects (line 12a). We also found that, instead of using the State Building Commission's records to identify the amount of non-federal matching expenditures to report on line 10j (related to construction projects), the department simply calculated the non-federal share based on an assumption that the federal share of expenditures was matched at a 21.3% rate. Calculating non-federal expenditures based on an assumption that the state matched federal expenditures at a predefined rate (instead of basing it on a review of expenditure records) represents a significant control deficiency, especially given the potential size of construction projects.

To determine whether the department had complied with the reporting compliance objectives, we reviewed the State Building Commission's records and determined for ourselves that the state provided the appropriate matching funds for the construction projects identified. By relying on an assumption of a predefined matching rate instead of the State Building Commission's records, the Accountant understated the non-federal expenditures related to construction projects in line 10j of the department's reports. For example, we noted that line 12a of the FFY 2015 SF-425 report submitted during our audit period was understated by $929,668. RSA relies on information reported to determine compliance with the matching requirement and to determine the amount of federal funds allowed to be obligated in the following year (carryover year). Underreporting non-federal expenditures ultimately understates the amount of federal funds the state can obligate in the carryover year.

Inadequate Controls and Noncompliance Related to Maintenance of Effort Requirements

The department is required to spend at least as much in non-federal expenditures as it spent two years prior. For instance, the department should have expended as much in non-federal expenditures in 2016 as it did in 2014. If the department does not meet that requirement, regulations require RSA to reduce the subsequent grant award by the deficit.

Based on discussion with the Department Controller, the controls for meeting the maintenance of effort requirement are the same as the controls over SF-425 reporting. Therefore, the internal control deficiencies related to reporting noted above are also internal control deficiencies over maintenance of effort.

We found that the maintenance of effort requirement for FFY 2016 was not met, and that RSA was unable to reduce the 2017 grant by the appropriate deficit because the SF-425 report for the FFY 2016 grant award was inaccurate. Specifically, based on the procedures performed, we determined that RSA should have reduced the FFY 2017 award by a total of $2,672,786 due to insufficient maintenance of effort expenditures. However, at the time of the audit, we could not identify evidence that demonstrated that RSA reduced the 2017 grant award due to the deficit in 2016 non-federal expenditures based on the department's submission of 2016 and 2014 SF-425 reports. This was likely due to the department not submitting a final SF-425 report for the 2014 award until the current audit period. In addition, RSA could not have reduced the 2017 award by the appropriate amount based on the 2016 and 2014 SF-425 reports fiscal staff submitted, because the 2016 SF-425 report was inaccurate, as described above. These inaccuracies would have led RSA to reduce the award by $2,361,323, which is $311,463 less than the required amount.

Risk Assessment

We reviewed DHS's November 2016 Financial Integrity Act Risk Assessment and determined that management addressed the risks associated with reporting inaccurate information on federal reports. However, the impact of the risk was assessed as high and the likelihood was assessed as remote, so no mitigating controls were described. Given the frequency with which we have identified reporting inaccuracies in the current audit and prior audits, we concluded that management should have assessed the likelihood as probable (high) and included a control activity to mitigate the risk in the department's annual risk assessment.

Criteria

According to Policy Directive 15-05 for line 10e. Federal Share of Expenditures,

> For reports prepared on an accrual basis, grantees should report Federal fund expenditures as the sum of cash disbursements for direct charges for goods and services, the amount of indirect expenses incurred, the amount of payments made to contractors/vendors, and the increase or decrease in the amounts owed by the recipient for goods received and services performed by employees, contractors/vendors, and other payees.

According to Policy Directive 15-05 for line 10f. Federal Share of Unliquidated Obligations,

> Enter the Federal portion of unliquidated obligations incurred by the grantee. Unliquidated obligations include direct and indirect expenses for goods and services incurred by the grantee, but not yet paid or charged to the VR grant award, including amounts due to contractors/vendors. When submitting a final SF-425 report, this line should be zero.

According to Policy Directive 15-05 for line 10j. Recipient Share of Expenditures,

> Enter the total amount of non-Federal VR expenditures incurred for the reporting period. This amount must include the grantee's non-Federal share of actual cash disbursements or outlays (less any rebates, refunds, or other credits), including payments to contractors, the grantee's non-Federal share of unliquidated obligations (reported separately on line 12d – Remarks), and the Non-Federal Share of Expenditures for the Establishment or Construction of Facilities for Community Rehabilitation Program (CRP) Purposes as reported on line 12a.

According to Policy Directive 15-05 for line 10l. Total Federal Program Income Earned,

> Enter the total amount of Federal program income (program income) earned and received by the grantee as of the end of the reporting period. Program income is considered earned in the fiscal year in which the funds are received by the grantee (34 CFR [*Code of Federal Regulations*] 361.63 and 2 CFR 200.80). Therefore, the amount reported on line 10l should not change after the grantee submits its fourth quarter SF-425 report.

According to Policy Directive 15-05 for line 10n. Program Income Expended in Accordance with the Addition Alternative,

> For those grantees using the addition alternative, enter the amount of program income that was used to supplement the Federal share of the total program costs. The amount reported on line 10n represents actual disbursements (i.e., outlays of program income by the grantee). The outlay of program income funds must meet

the same standards of allowability, reasonableness and allocability (2 CFR 200.403, 200.404 and 200.405) that are applicable to Federal funds (Section 108 of the Rehabilitation Act and 34 CFR 361.63(c)(3); and 2 CFR 200.307(e)(2), 200.401, and 200.408).

According to Policy Directive 15-05 for line 11c. Period From/To for Indirect Costs,

> Enter the beginning and ending effective dates for the approved indirect cost rate(s) or CAP.

According to Policy Directive 15-05 for line 11d-f. Base for Indirect Costs,

> d. Base: Enter the amount of the base against which the approved indirect cost rate(s) was applied. The base includes allowable expenditures to which the approved indirect cost rate may be applied. For CAPs, enter the total amount of the CAP costs (include both non-Federal and Federal).
>
> e. Amount Charged: Amount Charged (11b multiplied by 11d equals 11e): Data entry is not required for this field. This data element is calculated automatically.
>
> f. Federal Share: Enter the Federal share of the amount in 11e.

According to Policy Directive 15-05 for line 12a. Non-Federal Share of Expenditures for the Establishment or Construction of Facilities for Community Rehabilitation Program Purposes,

> Enter the non-Federal share of expenditures, also included in the total amount of non-Federal expenditures reported on line 10j, incurred for the establishment or construction of facilities for CRP purposes (34 CFR 361.62(b)). Only include those costs for activities that would meet the definition of "establishment of a facility for a community rehabilitation program" at 34 CFR 361.5(b)(18) and "construction of a community rehabilitation program" at 34 CFR 361.5(b)(12).

According to Policy Directive 15-05 for line *12d. Recipient Share of Unliquidated Obligations*,

> Enter that portion of unpaid obligations to be paid with non-Federal funds meeting the requirements in 34 CFR 361.60(b). This amount is also included in the amount reported on line 10j.

According to Policy Directive 15-05 for line 12f. Federal Program Income (VR SSA Payments Only) Transferred to the Independent Living Services for Older Individuals who are Blind (OIB) Program,

> Enter the amount of SSA payments received by the VR program and transferred to the OIB program (Section 108 of the Rehabilitation Act and 34 CFR 361.63(c)(2)

According to Title 29, *United States Code*, Section 731(a)(2)(B),

> The amount otherwise payable to a State for a fiscal year under this section shall be reduced by the amount by which expenditures from non-Federal sources under the State plan under this subchapter for any previous fiscal year are less than the total of such expenditures for the second fiscal year preceding that previous fiscal year.

Based on review of Title 2, *Code of Federal Regulations* (CFR), Part 200, Section 303(a), the department must

> Establish and maintain effective internal control over the Federal award that provides reasonable assurance that the non-Federal entity is managing the Federal award in compliance with Federal statutes, regulations, and the terms and conditions of the Federal award.

According to question seven of RSA's "Period of Performance FAQs," dated March 31, 2017,

> All expenditures incurred against an obligation must be tracked and reported by the States in terms of when the obligation was incurred, not when the liquidation occurs. For example, if a State enters into a contract in FFY 2016 for the provision of services under the VR program, thereby constituting an obligation for purposes of 34 CFR 76.707 for FFY 2016, but many of the invoices submitted by the contractor for payment will be submitted to the State agency during FFY 2017, the State VR agency must report those expenditures (i.e., liquidation of the obligations) on its SF-425s for FFY 2016, not FFY 2017 when the payments were made.

According to 2 CFR 200.403,

> Except where otherwise authorized by statute, costs must meet the following general criteria in order to be allowable under Federal awards:
>
> (a) Be necessary and reasonable for the performance of the Federal award and be allocable thereto under these principles.

Defining reasonable costs, 2 CFR 200.404 states,

> A cost is reasonable if, in its nature and amount, it does not exceed that which would be incurred by a prudent person under the circumstances prevailing at the time the decision was made to incur the cost.

Cause

The Vocational Rehabilitation reporting requirements are complex and differ from requirements for other federal programs, and the state has historically not prepared the reports properly. In the 2015 single audit, we noted that the department entered into a Corrective Action Plan with RSA in part to resolve the serious reporting deficiencies and noncompliance. During the prior audit, we were unable to test any reports, because RSA and DHS mutually agreed that DHS would not submit SF-425 reports until the Corrective Action Plan was fully implemented. It appears that at least some of the issues noted were the result of the department's eagerness to fully report transactions, which resulted in reporting transactions that occurred after the reporting cutoff date and inadvertently reporting duplicate transactions when the same transactions appeared in different information sources. Other issues were the result of misunderstanding the complex reporting requirements. The 2016 report that we tested was the first report that the department submitted for the Corrective Action Plan, and we noted significant improvement between that report and later reports.

Effect

In 2015, the Rehabilitation Services Administration identified the department's Vocational Rehabilitation program as high risk, for reasons including deficiencies in reporting and financial management. RSA also prescribed special conditions to the department's Vocational Rehabilitation program, including temporarily halting funding and requiring the state to complete a Corrective Action Plan with RSA. In addition to the risk of further funding disruptions, without accurate financial reporting, neither the state nor the federal awarding agency can make appropriate programmatic decisions based on the contents of reports.

Additionally, federal regulations address actions that may be imposed by federal agencies in cases of noncompliance. As noted in 2 CFR 200.338, "If a non-Federal entity fails to comply with Federal statutes, regulations or the terms and conditions of a Federal award, the Federal awarding agency or pass-through entity may impose additional conditions," including, as described in section 200.207, "Specific conditions":

> (1) Requiring payments as reimbursements rather than advance payments;
>
> (2) Withholding authority to proceed to the next phase until receipt of evidence of acceptable performance within a given period of performance;
>
> (3) Requiring additional, more detailed financial reports;
>
> (4) Requiring additional project monitoring;
>
> (5) Requiring the non-Federal entity to obtain technical or management assistance; or
>
> (6) Establishing additional prior approvals.

Furthermore, 2 CFR 200.338 also states,

> If the Federal awarding agency or pass-through entity determines that noncompliance cannot be remedied by imposing additional conditions [as described above], the Federal awarding agency or pass-through entity may take one or more of the following actions, as appropriate in the circumstances:
>
> (a) Temporarily withhold cash payments pending correction of the deficiency by the non-Federal entity or more severe enforcement action by the Federal awarding agency or pass-through entity.
>
> (b) Disallow (that is, deny both use of funds and any applicable matching credit for) all or part of the cost of the activity or action not in compliance.
>
> (c) Wholly or partly suspend or terminate the Federal award.

(d) Initiate suspension or debarment proceedings as authorized under 2 CFR part 180 and Federal awarding agency regulations (or in the case of a pass-through entity, recommend such a proceeding be initiated by a Federal awarding agency).

(e) Withhold further Federal awards for the project or program.

(f) Take other remedies that may be legally available.

Recommendation

The Department Controller should ensure that the Fiscal Director and Accountant are adequately trained with respect to reporting requirements for Vocational Rehabilitation, including RSA's instructions for report preparation, Vocational Rehabilitation regulations, uniform administrative guidance, and the terms and conditions of the grant award. The Department Controller should ensure that the internal controls for reporting for Vocational Rehabilitation are revised to provide for complete, accurate report submissions. This should include requiring fiscal staff to review records, including billing records related to program income and records related to construction projects, to ensure that all relevant financial activity is included in reports and has actually occurred. If there is no evidence demonstrating the transaction occurred during the reporting period, the transaction should not be included in a report.

The Department Controller should establish a documented process for calculating maintenance of effort thresholds based on actual expenditures and should ensure that DHS staff notify the U.S. Department of Education when the state's Vocational Rehabilitation Grants to States grant award should be reduced due to a maintenance of effort deficit.

The Commissioner of the Department of Human Services should assess all significant risks with sufficient attention to the impact and likelihood of the risk. The risk assessment and the mitigating controls should be adequately documented and approved by the Commissioner, who should implement effective controls to ensure compliance with applicable requirements, assign employees to be responsible for ongoing monitoring of the risks and any mitigating controls, and take action if deficiencies occur.

Management's Comment

We concur in part.

Management concurs that controls over the general reporting process need to be strengthened, and is in the process of making the revisions needed to result in what it believes will be complete and accurate report submissions. Management also concurs that portions of the SF-425 reports reviewed by the auditors were incomplete or inaccurate, but does not entirely agree with the auditors premise and the resultant dollars amounts detailed in items (A) through (F) of the finding. For example,

- Management agrees that errors were made in the calculation of and reporting of indirect costs, and will be refining the methodology used for reporting indirect costs for the report date ending September 30, 2018.

- Management agrees that journal entries should be made in a timelier manner so that they are posted by the time a report is filed and will be implementing controls to ensure this happens. It is important to note that the journals underlying the auditor-noted problem were in fact reclassifying expenditures and revenues that occurred prior to the report end date (September 30th or March 31st).
- Management also agrees that it needs to work more closely with its partnering state agencies to ensure that the appropriate information is obtained for capital projects and that obligations are made to the correct year.
- Management will add a calculation to the reporting template to formally indicate its consideration of the MOE requirement. The SF-425 is the mechanism in which management provides MOE information to RSA; therefore, a separate notification mechanism is not required. Additionally, Title 34 of the *Code of Federal Regulations* (CFR), Part 361, Section 62 (a), clearly states that the Secretary of Education is responsible for reducing the amount of the federal award. The department does not have any responsibility or authority in this regard.
- In relation to the duplicate billing and resulting questioned costs of $20,907, a journal entry was made in June 2017 to correct the duplicate billing. Therefore, the final SF-425 report for federal fiscal year 16 and the accounting records have been corrected.
- Management does not entirely agree with the premise and amounts included in items (A) through (F) pertaining to obligations and program income as detailed below.

Obligations

A significant amount of the dollars identified as incorrectly included in the report as obligations stemmed from multiyear contracts. The department enters into multiyear contracts in accordance with Central Procurement Office (CPO) standards for the state in order to realize discounts for goods and services. The contract summary sheets on these contracts clearly identify to which state year (and federal year indirectly) these costs will be obligated. Title 34 of the *Code of Federal Regulations* (CFR), Part 76, Section 707(c) states that an obligation is made "on the date on which the State or subgrantee makes a binding written commitment to obtain the services." The auditor's interpretation of this criteria is that the entire multiyear contract (5 years and longer in this case), should be obligated to the award year in which the contract was signed, which is problematic. The regulation is silent on whether the terms of the contract or the supporting documentation can stipulate to which year the obligation will be assigned. Additionally, the grant award only has a two-year period of performance and that is only if certain conditions are met to extend the initial one-year period of performance. Contract costs incurred after year 2 would then have to be charged to state dollars. Lastly, the auditor's interpretation does not appear to consider the provisions of 2 CFR 200 which requires a state to follow the same policies and procedures it uses for procurements from its non-federal funds. Management contacted the Central Procurement Office within the Department of General Services to gain clarity on those policies and procedures as they pertain to multiyear contracts. Correspondence from CPO stated, "As general best practices and procedures of CPO, agencies have purview to allocate and obligate their funding for a contract, even if it is a multi-year contract. It would be unduly burdensome and impractical to expect agencies at the time of the effective date to know how much of the funding they need for year five of a project and also to be unable to change distribution of funds from year to year." It should be noted that the department budgets out and obligates the entire 5-year contract for each year and obligates those funds accordingly.

Program Income

Program income variances noted by the auditor appear to be due to a misunderstanding of the system controls in place. Many of the discrepancies noted are instances in which program income was received during the reporting periods, but the cash was not settled until after the reporting period. For example, $100 was received on September 30, 2016; however, the cash impact was not settled until October 2, 2016. These are two separate considerations. One pertains to reporting and one pertains to cash management. See finding 2017-028 for management's response to cash management. When program income is received, the general ledger (Edison) automatically applies the income to expenses already incurred. In the event that enough expenses have not been incurred to cover the income received, a payable to the federal government is also recorded. Therefore, reporting program income as expended when received is an accurate reflection of the events that occurred, regardless of whether the cash is settled at a later date.

Risk Assessment

The department completes its annual risk assessment as required under *Tennessee Code Annotated*, Section 9-18-101 using guidance provided by the Tennessee Department of Finance and Administration (F&A). For the Department's November 2016 Financial Integrity Act Risk Assessment, risks of non-compliance were assessed by compliance type requirement for the Department as a whole. For the December 2017 Financial Integrity Act Risk Assessment, based on revised F&A guidance, risks were assessed on a more programmatic/divisional level.

Auditor's Comment

Obligations

While we recognize the challenges in adhering to the stipulations in 34 CFR 76.707(c), we are required to audit based on the regulations as written. If management wishes to apply numerous obligation dates to one contract, the department should obtain written federal approval of the approach. Additionally, there is no indication that the procurement requirements in 2 CFR 200.317 supersede Vocational Rehabilitation's period of performance requirements.

Program Income

In February 2018, subsequent to our audit fieldwork, we met with fiscal management to discuss the automated process to record and track the receipt and use of program income. After fiscal management provided a description of the automatic accounting entries, as well as, additional supporting documentation, we were able to confirm that most program income was expended by the end of the respective reporting periods. We, however, were unable to verify that all program income was expended as reported, because the automatic process for expending program income had not occurred for all program income receipts. Because the process appears to incur some delays, we could not conclude that program income was always expended as soon as received, as described by management.