# *Annual Audit Agenda*

## *June 30, 2008*

Georgia Department of Community Health

***Audited and Reported by a Joint Venture of Firms***

Metcalf Davis

Certified Public Accountants

Mauldin & Jenkins

Certified Public Accountants, LLC

## PURPOSE OF AGENDA

To address the overall ***independent auditors' report*** relative to fiscal year 2008.

To address certain ***required communications*** related to the fiscal year 2008 engagement.

To provide summarizations of ***findings and management letter comments*** related to the fiscal year 2008 engagement.

# GEORGIA DEPARTMENT OF COMMUNITY HEALTH

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**June 30, 2008**

## INDEPENDENT AUDITORS' REPORT

Significant excerpts from the Independent Auditors' Report include the following:

**A.** "**We have audited** the accompanying financial statements of the governmental activities, the business-type activities, each major fund and the aggregate remaining fund information of the State of Georgia's Department of Community Health (hereinafter referred to as the "Department of Community Health") as of and for the year ended June 30, 2008, which collectively comprise the Department of Community Health's basic financial statements as listed in the table of contents."

**B.** "These **financial statements are the responsibility of the Department of Community Health's management**."

**C.** "**Our responsibility is to express opinions** on these financial statements based on our audit."

**D.** "We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards,* issued by the Comptroller General of the United States."

**E.** **"We believe that our audit provides a reasonable basis for our opinions."**

**F.** "**In our opinion**, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, the business-type activities, each major fund and the aggregate remaining fund information of the Department of Community Health, as of June 30, 2008, and the respective changes in financial position, and where applicable, cash flows, thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America."

# REQUIRED COMMUNICATIONS

## ***The Auditor's Responsibility under Auditing Standards Generally Accepted in the United States of America and Government Auditing Standards***

As previously stated in our agreement with the State of Georgia's Department of Community Health (hereinafter referred to as the "Department") and as stated above, we would like the Department to understand our responsibility in connection with your audit.

Our audit of the financial statements of the Department for the year ended June 30, 2008, was conducted in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Department of Community Health's internal control over financial reporting. Accordingly, we express no such opinion. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and the significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinions.

In accordance with *Government Auditing Standards*, we have also performed tests of controls and compliance with laws and regulations that contributed to the evidence supporting our opinion on the financial statements. However, they do not provide a basis for opining on the Department's internal control or compliance with laws and regulations.

## ***Accounting Policies***

Management has the ultimate responsibility for the appropriateness of the accounting policies used by the Department. There were no significant new accounting policies or standards implemented this year. There are new accounting standards which will be required to be implemented in the coming years. These are discussed in the later in this document.

In considering the qualitative aspects of the Department's accounting policies, we did not identify any significant or unusual transactions or significant accounting policies in controversial or emerging areas for which there is a lack of authoritative guidance or consensus. The Department's policies relative to the timing of recording of transactions are consistent with GAAP and typical government organizations.

## ***Management Judgments and Accounting Estimates***

Accounting estimates are an integral part of the preparation of financial statements and are based upon management's current judgment. The process used by management encompasses their knowledge and experience about past and current events and certain assumptions about future events. Management has informed us they used all the relevant facts available to them at the time to make the best judgments about accounting estimates and we considered this information in the scope of our engagement. We considered this information along with the qualitative aspects of management's calculations in evaluating the Department's significant accounting estimates. Estimates significant to the financial statements include such items as the estimate for the valuation of benefit claims incurred but not reported, federal accounts receivable, over/under payment of claims, and allowance for doubtful accounts receivable.

## ***Financial Statement Disclosures***

The footnote disclosures to the financial statements are also an integral part of the financial statements. The process used by management to accumulate the information included in the disclosures was the same process used in accumulating the financial statements and the accounting policies described above are included in those disclosures. The overall neutrality, consistency, and clarity of the disclosures was considered as part our audit and in forming our opinion on the financial statements.

## ***Significant Difficulties Encountered***

Difficulties encountered in performing the audits are to include any serious difficulties that we encountered in dealing with management related to the performance of the audits. *Statements of Auditing Standards* issued by the American Institute of Certified Public Accountants (AICPA) defines "difficulties encountered" to include, but not limited to: unreasonable delays by management in providing needed information; unreasonable timetables set by management; and unavailability or lack of cooperation of client personnel in responding to appropriate audit inquiries.

We believe we received full cooperation of Department personnel, and believe we were given direct and unrestricted access to the Department's officials and the respective books and records. We experienced no significant difficulties (as defined in the above paragraph) in the performance of the fiscal year 2008 audit.

## ***Audit Adjustment***

As part of the Department's post-closing exercises, the Department made a significant amount of general ledger and financial statement adjustments. In accordance with generally accepted accounting principles (GAAP), an audit adjustment was necessary to properly reflect the Department's financial statements as of and for the fiscal year ended June 30, 2008.

The following is a summary of the June 30, 2008 audit adjustment proposed and recorded in the **general fund**:

| | Debits | Credits |
|---|---|---|
| | | |
| Reserved for Encumbrances | $ 7,419,886 | |
| Unreserved, Undesignated | | $ 7,419,886 |
| | | |
| *To reclassify fund balance from reserved for encumbrances to unreserved, undesignated based on our examination of encumbrances.* | | |

### *Uncorrected Misstatements*

We had no passed adjustments.

### *Disagreements with Management*

We encountered no disagreements with management over the application of significant accounting principles, the basis for management's judgments on significant matters, or significant disclosures to be included in the financial statements.

### *Representation from Management*

We requested written representations from management relating to the accuracy of information included in the financial statements and the completeness and accuracy of various information requested by us, during the audit. Management provided those written representations without a problem.

### *Management's Consultation with Other Accountants*

We know of no outside consultation by the Department or us in connection with our engagement, except as follows:

- The Department utilized the services of the Georgia Department of Audits and Accounts for internal auditing functions throughout the year,
- The Department utilized actuarial services of outside consultants for assistance in calculating the Medicaid and Employee Health Benefits claims incurred but not reported,
- The Department utilized the attestation services of other certified public accounting firms for purposes of providing attestation reports relative to the over/under payment of claims associated with payment accuracy of the Medicaid Management Information System (MMIS),

- We, likewise, utilized the services of an outside consultant for purposes of evaluating the Medicaid and Employee Health Benefits claims payable and the over/under payment of claims amounts as of June 30, 2008,
- The Department utilized the services of other certified public accounting firms for purposes of obtaining Statement on Auditing Standards (SAS) No. 70, *"Reports on Internal Controls in a Services Organization"* and reports for various aspects of the Department's operations. We reviewed those reports, and considered their effects on the financial audit,
- We, likewise, retained an independent CPA consultant, as provided in our contract, for ongoing assistance in planning and reviewing our audits as we deemed prudent.

## ***Significant Issues Discussed with Management***

There were no significant issues discussed with management related to business conditions, plans, or strategies that may have affected the risk of material misstatement of the financial statements. We are not aware of any consultations management had with us or other accountants about accounting or auditing matters. No major issues were discussed with management prior to our retention to perform the aforementioned audit.

## ***Other Information in Documents Containing Audited Financial Statements***

If you intend to publish or otherwise reproduce the Department's June 30, 2008 financial statements and make reference to either of our firms, we must be provided with printers' proofs or masters for our review and approval before printing. You must also provide us with a copy of the final reproduced material for our approval before it is distributed. We are not aware of any other documents that contain the basic financial statements. If such documents were to be published, we would have a responsibility to determine that such financial information was not materially inconsistent with the statements of the Department.

## ***Independence***

We are independent of the Department, and all related organizations, in accordance with auditing standards promulgated by the American Institute of Public Accountants and Government Auditing Standards, issued by the Comptroller General of the United States.

## ***Audit Firm Retention***

We know of no issues which would prevent us from performing next year's audits.

## ACCOUNTING RECOMMENDATIONS AND RELATED MATTERS

### Recommendations for Improvement

During our audit of the financial statements as of and for the year ended June 30, 2008, we noted areas within the accounting and internal control systems that we believe can be improved. We noted certain items as significant deficiencies in our supplemental reports on internal controls and compliance. Additionally, we noted certain items management should consider as part of its decision making process. Our recommendations (also commonly referred to as management points) are presented in the following paragraphs. Further, during our audit of the financial statements as of and for the year ended June 30, 2008, we noted other matters which we wish to communicate to you in an effort to keep the Department abreast of accounting matters that could present challenges in financial reporting in future periods. We believe consideration of these recommendations will help provide proper control over financial activities, and add effectiveness and efficiency to overall operations.

### Significant Deficiencies

As noted in our supplemental reports on internal controls and compliance, we reported the following significant deficiencies:

1. **Verification and Documentation of Eligibility *(This is a modification and partial repeat of finding SA 07-02 and this is considered to be a material weakness)***

   The Department is responsible for administering the State of Georgia's Medicaid program. The Medicaid program is overseen by the U.S. Department of Health and Human Services through the Centers for Medicare and Medicaid Services (CMS). The Department is also responsible for determining that all recipients meet prescribed eligibility requirements and those requirements are appropriately documented.

   This is a modification and partial repeat of finding SA 07-02 from the year ended June 30, 2007. The Department has contracted with the Department of Family and Children Services (DFCS) to provide enrollment and monitoring services for Medicaid members. During fieldwork we noted six instances in a sample of 60 of Medicaid recipients whose eligibility was not properly documented. Those six instances were as follows:

   a. Two case files were not able to be located by the Department.
   b. Two case files did not contain evidence that eligibility was recertified in accordance with the policies and procedures in place.
   c. One case file did not contain acceptable proof of identification.
   d. One case file was not signed or dated by the recipient.

The Department does not have an adequately effective monitoring process in place over DFCS to ensure that all CMS guidelines in regards to the documentation of a member's eligibility are properly followed.

The Department should improve their verification and documentation monitoring policy for Medicaid members and create more stringent controls over the eligibility process.

**2. Federal Accounts Receivable *(This is considered to be a material weakness)***

The Department is responsible for accurately reporting accounts receivable in the annual financial statements. As part of that responsibility, the Department is required to reconcile amounts reported in the financial statements to amounts recorded in the general ledger as well as to other special reports. The very nature of a reconciliation process involves justifying and verifying amounts that are considered to be reconciling items. Reconciliation of the respective amounts should be performed periodically and timely, and the process and results thereof should be reviewed and adequately supervised. The preparer should seek assistance and consultation when warranted.

As part of the audit process, we requested support for the amount of accounts receivable due from the federal government reflected in the Department's financial statements. We received a calculation/reconciliation from Department personnel which attempted to support the amounts reported in the respective financial statements.

During our analysis of the reconciliation, we noted certain reconciling descriptions and amounts approximating $73 million which did not appear to be appropriate. We discussed the matter with the individual responsible for the reconciliation; however, we were not satisfied with the response. Upon further analysis, we were able to determine certain amounts reflected in the reconciliation could not be supported and should not be included in the reconciliation, and other reconciling amounts which were required had been omitted or inaccurately shown in the reconciliation.

Subsequent to our determination of the problems and the respective resolutions, the party responsible for the reconciliation acknowledged the fact that incorrect information was used due to an inability to determine the correct information.

The Department did not properly approach the need for reconciling amounts due from the federal government. We noted the fact that one individual was involved in the preparation of the reconciliations for which we observed no evidence of adequate supervision, consultation or review. Further, the party responsible did not adequately understand the accounting matters affecting the reconciliation process, and the ultimate need to verify and justify all reconciling items.

We recommend the Department consider the following:

- Place people in positions commensurate with their experience, knowledge, and ability.
- Train and cross-train those personnel on the responsibilities of their position(s).
- Emphasize the need for responsible personnel to consult with others in the Department when the situation dictates.
- Perform a better and more complete reconciliation process of the accounts receivable. This requires a change in certain elements of the conceptual framework currently being performed.
- Require reconciliations of accounts receivable be performed at least quarterly.
- Stress the need for accountability, and the fact that all efforts must be justifiable and verifiable.
- Supervise, manage and review the results and efforts of individuals, and challenge the responsible parties on the propriety of information.

### 3. Reserve for Encumbrances

The Department is responsible for accurately reporting reservations of fund balance. A reserve for encumbrances should be reported when a commitment resulting from a contract, purchase order, salary agreement, travel claim, or other such commitments remains unsatisfied and the actual expenditure will be made after year-end. Amounts which represent liabilities as well as amounts for which the commitment no longer exists should not be reflected as a reserve for encumbrances.

We noted management initially encumbered $102 million of funds which were also reported as payables at June 30, 2008. During our examination of the remaining encumbrances, we noted purchase orders related to contract commitments which no longer existed or were applied to the wrong fiscal year. Four purchase orders totaling $7 million or roughly 7% should have been unencumbered prior to year-end and two purchase orders totaling $3.6 million of fiscal year 2009 expenditures were inappropriately applied to fiscal year 2008 encumbrances.

The Department's controls did not include routine formal documentation from the appropriate contract business owners to the financial services area supporting the need to maintain encumbrances. Additionally, the procedures used to document a contract termination or renewal were not always fully utilized to communicate amounts which should remain encumbered.

We understand management's reluctance to release encumbrances when the potential exists that a future invoice may yet be presented for payment. However, we recommend the Department enhance and formalize routine communication with contract business owners to ensure encumbrances are released for commitments which no longer exist or have been satisfied.

## Management Points

We have discussed various matters with management pertaining to operations and controls including, but not limited to:

### 4. Cash Receipts – Financial Services

The Department utilizes a series of lock boxes to collect the majority of its cash receipts. Nonetheless, more than $73.5 million in checks and cash were received directly by the Department's Financial Services Division during fiscal year 2008. The majority of the amounts were opened and keyed into a spreadsheet by one employee. However, not all amounts received were included on the spreadsheet. While we did not note any discrepancies, the cash receipts data on the spreadsheet is not being compared to bank deposits or amounts recorded in the general ledger. Additionally, we noted the spreadsheet is maintained on the employee's local hard drive which is not routinely backed-up.

We recommend the Department's management implement stronger, more formal policies and procedures related to cash receipts received directly by the Department's Financial Services Division. Such policies and procedures should require all amounts be included on the spreadsheet and compared periodically to bank deposits or amounts recorded in the general ledger. Additionally, data files important to the Department's internal control should be maintained where data is routinely backed-up.

### 5. Cash Receipts – Mail Room

As a result of certain inquiries we noted, despite the best efforts of the Department, various payments are periodically received by the mailroom personnel rather than through the appropriate channels. When the envelope for the mailings does not indicate a designated recipient or division, mailroom personnel open the mailing in order to facilitate delivery. When the contents of the mailing identify a recipient, the check is delivered to that individual or division. When the contents of the mailing do not identify a recipient, the check is delivered to an administrative assistant in the Financial Services Division. We commend the Department for developing procedures in which the mailroom electronically tracks cash receipts and delivery of cash receipts to the appropriate Department personnel. In an effort to improve internal control, we recommend the Department's mailroom personnel routinely provide this listing to accounting so they may ensure proper deposit of these funds.

## 6. Internal Auditor

We noted the State Health Benefit Plan (the "Plan") was allocated two full time internal audit positions which were filled subsequent to year-end. We encourage management to train and begin utilizing these personnel to perform audits of the Plan's payroll locations as soon as possible. We feel this is an important part of the State Health Benefit Plan's monitoring process.

## 7. Testing of Service Providers' Relevant Internal Controls

We noted the Department relies frequently on outside entities to provide services which are critical to the Department's objectives. As a matter of policy, the Department requires assurance from independent sources that relevant internal controls at its service providers are in place and functioning. We noted two service providers for which the Department has not recently received such assurance. The State Accounting Office and the Georgia Technology Authority both provide services which are critical to the Department's objectives to provide timely, accurate and reliable financial information. During fiscal year 2008 we understand the Georgia Department of Audits and Accounts performed a follow-up review of the current status regarding findings and recommendations reported by an outside consultant based on a security review of the operating systems and network devices of the Georgia Technology Authority and the State Data Center.

The Department is expected to participate in the Georgia Infrastructure Transformation (GAIT) 2010 which will result in an outsourcing to external service providers both IT infrastructure and telecommunications delivery beginning in 2010.

In an effort to ensure the quality of services received by the Department, we recommend management require assurance from all independent outsourced parties that relevant internal controls are in place and functioning for such service providers.

## 8. Collateralization of Deposits

At June 30, 2008, the Department had approximately $20 million in uninsured deposits with private financial institutions. As of June 30, 2008, the private financial institutions were not required to provide collateral for these excess deposits. This places significant Department funds at risk in the event of financial institution failure. Subsequent to year end, efforts have been made to formalize agreements with certain financial institutions which would provide collateralization of uninsured deposits. We recommend management require all financial institutions where accounts are maintained to provide collateral for the Department deposits in excess of the amounts insured by the Federal Deposit Insurance Corporation (FDIC).

**9. Member Enrollment Management System (MEMS) Controls**

Within the Department's current MEMS, there is a data screen where changes to multiple eligibility records can be made. Access to this screen is limited to specific users within the Department. We understand the Department is in the process of converting the current MEMS to a DB2 system and there are plans for the new system to show all modifications by users. Additionally, management plans to develop policies and procedures to examine and audit individual eligibility files accessed by users of the new MEMS after conversion.

Although access is limited to specific users of the current MEMS, we recommend the Department develop policies and procedures to ensure employees with access do not make unauthorized modifications. These policies and procedures may include examining specific user eligibility files on a regular basis to ensure MEMS agrees with the user's eligibility file. Formal documentation of these procedures should be maintained for a reasonable period of time to support the control.

**10. Vendor Management Controls**

Our audit included testing the controls and procedures of the Department's Vendor Management during fiscal year 2008. We tested 20 of the 198 contracts monitored and four of the 12 site visits conducted during the year ended June 30, 2008. As a result of our test work, we noted significant improvement in the monitoring controls and procedures in place and functioning. However, we noted the site visit checklist was missing from one monitoring file and two site visit acknowledgement letters were not sent within the 45 day timeframe requirement according to Vendor Management policy.

We understand the delay in sending the acknowledgement letters as well as the lack of the completed checklist resulted from employee terminations during the year. Both employees terminated their employment with the Department prior to completing the necessary documentation. We recommend management develop policies and procedures which would ensure all necessary documentation be completed prior to an employee's termination. Such policies and procedures could include close monitoring of work assignments by contract managers prior to the employee's separation.

**11. Non Claim Transactions**

The Department has a policy in place for initiating, authorizing and reconciling financial transactions which are not claim specific. Management utilizes an Accounting Transaction Request (ATR) form to authorize Affiliated Computer Services (ACS) to process non claim specific financial transactions such as adjustments to receivables from providers. While we noted no transactions that were not properly authorized during fiscal year 2008, the Department was not adhering to all steps set forth in the policy. Additionally, we noted the policy could be modified to strengthen internal control. We recommend management modify the policy to enhance the reconciliation of requested transactions to those actually processed by ACS to ensure no transactions are processed outside of the established procedures. Further, we recommend the Department adhere to all steps of the ATR policy.

**12. State Health Benefit Plan Dependent Documentation**

During our procedures, we tested 30 State Health Benefit Plan claims paid during the year ended June 30, 2008 by the Department. For three of those claims, management was unable to locate documentation supporting dependent eligibility. We understand the documentation supporting dependent eligibility received prior to September 2008 is stored off site and is often difficult to locate. Nonetheless, we recommend all documentation supporting eligibility be accessible in a timely manner.

We further understand the Department began to utilize a scanning system in September 2008 and all dependent verification documents currently received by the State Health Benefit Plan are scanned. Scanning should improve the efficiency of locating such documents in the future, and we recommend the Department consider scanning documents supporting dependent eligibility which were received prior to September 2008.

**13. Intergovernmental Receivables**

During our testing of intergovernmental receivables we noted amounts in the year-end balance that had no collections or activity in the fiscal year ended June 30, 2008. Additionally, certain amounts appeared uncollected from fiscal year ending prior to June 30, 2007. There is no allowance for these receivables and there does not appear to be procedures in place to periodically review these amounts for collectibility. We recommend the Department establish procedures to ensure the intergovernmental receivables are routinely reviewed by management and an allowance is established as necessary to reserve any amounts which may not be fully collectible.

## Other Matters

During our audit of the financial statements as of and for the year ended June 30, 2008, we noted other matters which we wish to communicate to you in an effort to keep the Department abreast of accounting matters that could present challenges in financial reporting in future periods.

**14. New Audit Standards -** The American Institute of Certified Public Accountants (AICPA) has been very busy over the past several years with the issuance of several new auditing standards, which should be of interest to the Department.

A series of eight (8) new audit standards commonly known as SAS's 104 – 111 Risk Assessment Standards were issued by the AICPA in March 2006 relating to risk assessment involved in the planning and performance of a financial statement audit. One of the major changes resulting from these new standards is the requirement for auditors to gain a more in-depth understanding of the client and its operating environment, including its internal controls. In the past, auditors were only required to gain an understanding of internal controls; whereas, auditors are now required to evaluate the design of relevant controls and determine whether these controls have been placed into operation. To make this determination, auditors are now required to test controls even when they plan to place no reliance on them during the performance of the audit.

These new audit standards also require more detailed documentation than previously issued standards. We adopted the above audit standards with this audit of June 30, 2008, and modified our audit approach in order to implement these new standards in an effective and efficient manner.

**15. <u>New GASB Standards</u>** - As has been the case for the past 10 years, GASB has issued several other new pronouncements which will be effective in future years. The following is a brief summary of the new standards:

a. Statement No. 49, *Accounting and Financial Reporting for Pollution Remediation Obligations*, addresses liabilities for existing pollution remediation projects as they are discovered and acted upon. This is effective for the Department with fiscal year ending June 30, 2009.

b. Statement No. 51, *Accounting and Financial Reporting for Intangible Assets*, which establishes accounting for assets such as easements, water rights, trademarks, and internally generated computer software. This is effective for the Department with fiscal year ending June 30, 2010.

c. Statement No. 52, *Land and Other Real Estate Held as Investments by Endowments*, establishes consistent standards for the reporting of land and other real estate held as investments by essentially similar entities. It requires endowments to report their land and other real estate investments at fair value. This pronouncement is effective for the Department with fiscal year ending June 30, 2009, but it should not have any real effect based on the current financial condition of the Department.

d. Statement No. 53, *Accounting and Financial Reporting for Derivative Instruments*, which is intended to improve how governments report information about derivative instruments in their financial statements. Specifically, it requires governments to measure most derivative instruments at fair value in their financial statements. It also addresses hedge accounting requirements to determine whether a derivative instrument results in an effective hedge. This is effective for the Department with fiscal year ending June 30, 2010.

**Summations of Thoughts Noted Above**

We believe the implementation of these suggestions will enhance both the control environment and the financial reporting process, making both more effective. We also believe these recommendations can be easily implemented, and all problems resolved quite timely should management elect to employ the corrective measures.

## CLOSING

If you have any questions regarding any comments, suggestions or recommendations set forth in this memorandum, we will be pleased to discuss it with you at your convenience.

This report is intended solely for the information and use of the Board, the audit committee, management of the Department, federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

We appreciate the opportunity to serve the Department of Community Health and look forward to serving the Department in the future. If we could be of further assistance, please feel free to call upon us.