Annual Audit Agenda

Summary of Information & Communications:
Annual Financial & Compliance Audit
As Of and For the Year Ended June 30, 2011

Georgia Department of Community Health

Audited and Reported by a Joint Venture of
Certified Public Accounting Firms

Metcalf Davis
Certified Public Accountants

Mauldin & Jenkins
Certified Public Accountants, LLC

GEORGIA DEPARTMENT OF COMMUNITY HEALTH

Annual Audit Agenda

June 30, 2011

PURPOSE OF AGENDA

To share information about the ***engagement team***.

To share information about the ***audit process and deliverables timeline***.

To address the overall ***independent auditors' report*** relative to fiscal year 2011.

To provide a ***summary overview of the financial statements & footnotes*** of fiscal year 2011.

To address certain ***required communications*** related to the fiscal year 2011 engagement.

To provide summarizations of ***findings and management letter comments*** related to the fiscal year 2011 engagement.

ENGAGEMENT TEAM

Metcalf Davis / Mauldin & Jenkins:

- Large regional joint venture audit organization serving the Southeastern United States.
- Multiple offices located in:
    - **Georgia:**
        - Atlanta
        - Macon
        - Albany
    - **Alabama:**
        - Birmingham
    - **Florida:**
        - Bradenton
- Serve more governmental entities in the Southeast USA than any other certified public accounting firm requiring over 65,000 hours of service on an annual basis. Provider of over 300,000 hours of service to all clients on an annual basis.
- Most recent auditor of approximately 200 total governmental entities, and also serves another 250 not-for-profit entities. The solid majority of these governmental and not-for-profit entities receive substantial federal funding.
- Firms are the auditor of a very large and substantial part of the State of Georgia including approximately 25% of the State's general fund, and the solid majority of the State of Georgia's component units, including the audit of the State of Georgia's Department of Audits & Accounts.
- Auditors of entities with assets as much as $5 billion.

ENGAGEMENT TEAM

Engagement Team Leaders on the Audit Engagement Include:

- **Miller Edwards**, Engagement Partner - 26 years experience serving governments with 12 years experience auditing the Department of Community Health (the "Department").
- **Greg Davis**, Quality Assurance Partner - 36 years experience serving governments with 12 years experience auditing the Department.
- **Matt Hill**, Manager (Compliance = Single Audit) - 13 years experience serving governments with 12 years experience auditing the Department.
- **Donarene Steele**, Manager (Financial Audit) - 20 years experience serving governments with 7 years experience auditing the Department.
- **Clayton Knox**, Manager (Financial Audit) - 10 years experience serving governments with 7 years experience auditing the Department.
- **Marci Thomas**, Manager (Compliance & Financial Audits) - 25 years experience serving governments with 2 year experience auditing the Department.
- **Joel Black**, Quality Assurance Partner - 18 years experience serving governments with 1 year experience auditing the Department.
- **Meredith Lipson**, Quality Assurance Partner (Compliance) - 22 years experience serving governments with 11 years experience auditing the Department.

OVERVIEW OF AUDIT PROCESS & DELIVERABLES TIMELINE

The following information presents a small timeline of certain significant events in the conduct of the annual financial and compliance audit:

- **April 29, 2011** Audit engagement letter executed by Commissioner.
- **May 6, 2011** Management provided a projected annualized Schedule of Expenditures of Federal Award (SEFA). Single Audit planning commenced.
- **May 16, 2011** First audit status meeting, and initial audit plan was theorized with management. We began the annual audit process focusing on the compliance and planning elements of the audit.
- **August 11, 2011** Met with Audit Committee and shared audit plans, timeframes and schedules. Key dates were shared with **October 14, 2011** as key date for management providing the financial statements, notes and SEFA for audit. Updated this communication with Audit Committee on **October 13, 2011**, and management affirms the key date will be met.
- **October 19, 2011** Received revised SEFA which prompted two (2) additional major program audits (subsequently revisions through November 17, 2011).
- **November 2, 2011** Management provided adjusted general ledgers and draft financial statements and notes for audit (subsequently revisions by management on several occasions through November 17, 2011)
- **November 18, 2011** We provided requested oral affirmations to State Accounting Office.
- **November 21, 2011** We concluded our financial and compliance audits based on information provided by Department management, and all of our reports (deliverables) are dated this date which was our last day of fieldwork as well as the completion of our extensive quality assurance and review process.

INDEPENDENT AUDITORS' REPORT

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

A. **Scope:** "**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, 2011, which collectively comprise the Department of Community Health's basic financial statements as listed in the table of contents."

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

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

D. **Audit Standards:** "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. **Clean Opinion:** "**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, 2011, 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."

OVERVIEW OF FINANCIAL STATEMENTS AND FOOTNOTES

Statement of Net Assets (Page 4) – This statement is similar to a balance sheet, and presents the governmental and business-type activities of the Department of Community Health (hereinafter referred to as the "Department") as of June 30, 2011. The statement is prepared under the full-accrual method of accounting and includes components for capital assets and long-term debt. The governmental activities are primarily the Medicaid activities of the Department, and the business-type activities surround the State Health Benefit Plan (SHBP).

Significant elements to consider as of June 30, 2011 include:

- Cash and cash equivalents amount to approximately $91 million as of June 30, 2011 as compared to $83 million as of June 30, 2010. Consequently, cash and cash equivalents decreased by approximately $8 million during 2011. Further, over a three (3) year period, cash and cash equivalents have decreased by approximately $600 million since June 30, 2008. Most of the cash reduction was in the SHBP.

- Total receivables amount to approximately $920 million as compared to $1.15 billion as of the close of the prior fiscal year. This results in a decrease in receivables during 2011 in the approximate amount of $230 million.

- Total assets amount to approximately $1.040 billion versus the prior year approximation of $1.265 billion. Therefore, total assets have decreased by approximately $225 million.

- Liabilities include the usual items such as accounts payable, accrued liabilities and benefits payable. One of the more significant obligations includes current liabilities of cash overdrafts and accounts payable and other accruals which (in total) approximated $390 million as compared to $365 million in the prior year. Additionally, benefits payable approximated $910 million as of June 30, 2011 as compared to $970 million as of June 30, 2010. The benefits payable consists primarily of actuarially calculated amounts for the respective incurred-but-not-reported (IBNR) liabilities for the payment of claims.

- Total liabilities approximated $1.393 billion as of June 30, 2011 as compared to $1.465 billion as of June 30, 2010.

- During 2011:
  - Assets decreased by approximately $225 million;
  - Liabilities decreased by approximately $72 million;
  - Net Assets ended in a deficit of approximately $357 million as compared to the prior year deficit of approximately $200 million.
  - Governmental activities represented a deficit of approximately $174 million while the Business-Type Activities (SHBP) represented a deficit of approximately $183 million.
  - Total Net Assets decreased across activities by approximately $157 million.

Statement of Activities (Page 5) – This statement is intended to report the operations of the Department based on its primary functions and programs. It is reported on the full-accrual basis of accounting and is certainly a unique presentation as required by governmental financial reporting standards.

Significant elements to consider for the year ended June 30, 2011 include:

- The governmental activities primarily surround the Medicaid Program and Children's Health Insurance Program (CHIP) programs as well as numerous programs that transitioned with divisions of the former Department of Human Resources (DHR). The business-type activities represent activities of the SHBP.

- **Revenues.** Total revenues (program and general revenues) amounted to approximately $11.953 billion as compared to $11.583 billion in the prior year. This represents an increase of approximately $370 million or 3.2%. A further breakdown and comparison is as follows:

	FY 2011	FY 2010	Change
Charges for Services	$ 2,406,000,000	$ 2,136,000,000	12.6%
Operating Grants	6,484,000,000	6,742,000,000	(3.8%)
State Appropriation	2,233,000,000	2,099,000,000	6.4%
Other General Revenues	830,000,000	606,000,000	37.0%
Total Revenues	**$11,953,000,000**	**$11,583,000,000**	**3.2%**

- Program revenues (second and third columns) are those revenues received and earned that directly offset the functional expenses. Program revenues (charges for services and operating grants) amounted to approximately $8.9 billion as compared to $8.9 billion in the prior year. Therefore there was no increase or decrease in program revenues between years.

- General revenues primarily include the State Appropriations, other revenue collections, and intergovernmental transfers, and such amounts totaled approximately $2.2 billion for the fiscal year ended 2011.

- **Expenses.** Total expenses (first column) amounted to approximately $12.110 billion as compared to $11.811 billion in the prior year. This represents an increase of approximately $300 million or 2.5%. A further breakdown and comparison is as follows:

	FY 2011	FY 2010	Change
Education	$ 54,000,000	$ 43,000,000	25.6%
Health & Welfare - Public	9,426,000,000	9,265,000,000	1.7%
Contribution to State	406,000,000	205,000,000	98.0%
Health & Welfare – State Health Benefit Plan	2,224,000,000	2,298,000,000	(3.2%)
Total Expenses	**$12,110,000,000**	**$11,811,000,000**	**2.5%**

- Federally Funded expenses/expenditures amounted to approximately $6.750 billion or 56% of all of the above expenses.

- **Change in Net Assets.** In the end, the change in Net Assets represents the current fiscal year shortage of revenues versus expenses in the approximate amount of $157 million. The change in net assets (net loss) continues to be a negative amount on Net Assets for which fiscal year 2010 experienced a shortfall of approximately $228 million. Consequently, the Department has reported losses from overall operations over the past two (2) years in the approximate amount of $385 million.

General Fund Financial Statements (Pages 6 – 8) – Such statements include a balance sheet and a statement of revenues, expenditures and changes in fund balance. These statements follow accounting standards, and use the modified accrual method of accounting. Reconciliations from the modified accrual to full-accrual basis of accounting are reported at the bottom of page 6 and also on page 8.

Proprietary Fund Financial Statements (Pages 9 – 11) – Such statements include a statement of net assets and a statement of revenues, expenses and changes in net assets. These statements follow accounting standards, and use the full-accrual method of accounting. A statement of cash flows is included, and it reflects the sources and uses of cash and cash equivalents.

Fiduciary Fund Financial Statements (Pages 12 – 13) – Such statements include a statement of net assets and a statement of changes in fiduciary net assets relative to post employment health benefits. These statements follow accounting standards, and use the full-accrual method of accounting.

Footnotes (Pages 14 – 35) – The more significant footnotes are discussed below:

Note 1 – Summary of Significant Accounting Policies. This footnote discusses the overall Department, and the nature of its operations. This footnote also shares with the reader of the financial statements the significant accounting policies and principles utilized in the preparation of the financial statements.

Note 2 – Deposits and Investments. This footnote discloses common deposit and investment risks related to credit risk, concentration of credit risk, and interest rate risk. The footnote also addresses collateralization of bank deposits.

Note 3 – Accounts Receivable. Information regarding receivables and allowances for bad debts are discussed in this footnote.

Note 4 – Capital Assets. This footnote provides information relative to the buildings and equipment owned and occupied by the Department and reflects changes to opening balances relative to the DHR transition.

Note 9 – Risk Management. This footnote provides details on how the Department manages risks for which it is exposed.

Note 11 – Other Postemployment Benefits (OPEB). Substantial information is disclosed in this footnote about the Department's administration of the defined benefit postemployment healthcare plan.

Note 12 – Retirement Systems. Disclosure is provided about the Department's participation in the various retirement plans administered by the State.

Required Supplementary Information (Pages 36 – 42) – Governmental Accounting Standards Board (GASB) pronouncements require certain supplemental information with the basic financial statements. A summary of this information is provided below:

Schedules of Funding Progress and Employer Contributions (Page 36 and 37). As required by GASB, information is disclosed regarding the State's other post employment benefit plan.

Budget Comparison Schedules, Reconciliations, and Notes (Pages 38 – 42). As required by GASB, this information attempts to share information regarding budget to actual amounts on a budget basis and then reconciled to GAAP.

OVERVIEW OF COMPLIANCE REPORTS

As part of the annual audit process, we have performed a substantial compliance audit and Single Audit of the programs which are federally funded. For the year ended June 30, 2011, total expenditures of federal awards amounted to approximately $6.750 billion. ARRA funded expenditures amounted to approximately $586 million as compared to $732 million in the prior year. Federally funded expenditures approximated 56% of total Department expenditures.

We have issued two (2) reports which are required by *Government Auditing Standards* and they are in a separate package from the financial statements. <u>We reported fourteen (14) findings (material weaknesses and significant deficiencies) relative to the Department's lack of internal controls and noncompliance with certain Federal programs' rules and regulations</u>.

The Single Audit compliance testing covered seven (7) major programs as follows:

1) $5.864 billion	-	Medicaid Cluster
2) $158 million	-	Immunization Cluster
3) $229 million	-	State Children's Healthcare Insurance Program
4) $28 million	-	Public Health Emergency Preparedness
5) $43 million	-	HIV Care Formula Grants
6) $291 million	-	Special Supplemental Nutrition Program for Women, Infants, and Children
7) $21 million	-	Early Intervention Services (IDEA) Cluster (a/k/a as Babies Can't Wait)
$6.634 billion	**-**	**Total Federal Expenditures Tested Under the Provisions of the Single Audit Act of 1984**

We have also issued a management letter with further recommendations for improvement in the areas of internal control, compliance and general operations. <u>We reported thirty-three (33) recommendations to the Department in the management letter</u>.

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 Department and as stated above, we would like everyone to understand our responsibility in connection with your audit.

Our audit of the financial statements of the Department for the year ended June 30, 2011, 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'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 other than Governmental Accounting Standards Board (GASB) No. 54, *"Fund Balance Reporting and Governmental Fund Type Definitions,"* which changes the terminology and reporting relative to the presentation of fund balance in governmental funds at the fund level. There are new accounting standards which will be required to be implemented in the coming years. These are discussed 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 generally accepted accounting principles (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 in Performing the Audit

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 2011 audit.

Audit Adjustments

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 GAAP, a series of audit adjustments were necessary to properly reflect the Department's financial statements as of and for the fiscal year ended June 30, 2011. Such adjustments surrounded amounts computed and recorded relative to:

a) Various Federal receivables and offsetting deferred revenues;
b) Accounts payable (see Finding FS 11-03)
c) Benefits payable at the State Health Benefit Plan and the respective fiduciary funds (see Finding FS 11-04);
d) Provider receivables; and,
e) Allowance for doubtful accounts.

See various management letter comments that address several of the above audit adjustments.

Uncorrected Misstatements

We had one (1) passed adjustment. The passed adjustment had no fund balance effect and no bottom-line change to the operating statement. The passed amounts simply affected assets and liabilities of the same amount, and the revenues and expenses by the same amount.

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 & Accounts (DOAA) for internal auditing functions throughout the year as well as the performance of an attestation engagement relative to the Department's Budget Comparison Reports (BCR);
- The Department utilized actuarial services of outside consultants for assistance in calculating the Medicaid (governmental activities) and Employee Health Benefits (business-type activities) claims IBNR;
- 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, 2011;
- 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);
- 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;

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, 2011 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 AICPA 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, 2011, we noted areas within the accounting and internal control systems that we believe can be improved. We noted certain items as material weaknesses and 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, 2011, 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.

Material Weakness

1. **Controls Over Upper Payment Limit Calculation (Substantial Repeat of Prior Year Finding)**

   Title 42 of the Code of Federal Regulations, sections 447.272 for hospital inpatient services and 447.321 for hospital outpatient services, nursing homes, physician groups and intermediate care facilities for mental retardation (ICF-MR), states that the Department is eligible to calculate Upper Payment Limit (UPL) for providers that are state government, non-state government and privately owned and operated facilities. UPL refers to a reasonable estimate of the amount that would be paid for the services furnished by the group of facilities under Medicare payment principles.

The Department's management is responsible for implementing and maintaining adequate controls to ensure a reasonable estimate of the amount is accurately computed. A detail review of the calculation by someone independent of the calculation process is a necessary part of ensuring the reasonableness of the estimated UPL amount.

At June 30, 2010, the Department recorded a preliminary estimate for inpatient and outpatient UPL as the final estimated calculation and payment had not been completed for the 2010 fiscal year. The actual calculation for the 2010 fiscal year was completed and paid during fiscal year 2011; however, the actual payments were approximately $15 million less than the June 30, 2010 accrual. The difference in the estimate and actual payment related to State of Georgia (State) plan amendment changes as well as revisions to certain ratios. The State plan amendment changes and information used to calculate the ratios was however available to the Department at the time the estimate was calculated.

Management concurred with the prior year finding and indicated they would contract with the DOAA to provide support and data validation for all hospital, nursing home and physician UPL payments. Further, management indicated that the DOAA review would precede the submission of sample calculations to Centers for Medicare & Medicaid Services (CMS) and would include verification of source data used in the various UPL calculations.

During fiscal year 2011, the Department made UPL payments for hospital inpatient and outpatient services, nursing homes, physician groups and ICF-MR prior to having the calculations reviewed by the DOAA. Additionally, there was no indication of a detailed review performed by Department management.

During the annual audit of the Department, officials maintained that the DOAA had performed such detail reviews on current fiscal year 2011 calculations and payments, but after extensive inquiries and observations, it was determined that those reviews were made on prior year estimates and not for current year calculations and total payments. Consequently, UPL payments were transacted without an independent review by appropriate parties prior to release of payments.

Material adjustments to the UPL amounts have occurred in previous years as a result of our audit work. For the past several years, total UPL calculated amounts have averaged approximately $200 million per year.

The accrual of inpatient and outpatient UPL at June 30, 2010 was overstated by approximately $15 million. Total UPL payments for accrued amounts as of June 30, 2010 as well as amounts expensed relative to the year ended June 30, 2011 of approximately $285 million were disbursed during the fiscal year ended June 30, 2011 prior to undergoing a detailed review by the DOAA or Department management.

It is imperative that management develop adequate procedures to review its UPL calculations in detail in order to ensure the amounts paid as well as the amounts recorded in the Department's financial statements are properly supported, reviewed and represent management's best estimate. This process should include a detailed review of supporting documentation to ensure the data used in calculating UPL is accurate and in accordance with the applicable UPL State plan.

Management may decide to ask a third party to review and validate data for all UPL calculations. However, the responsibility for the accuracy of the estimate still rests with management. Therefore, it is necessary that management and the third party have a thorough understanding of the procedures to be performed by the third party. These procedures should be formally documented and management should review the output to ensure they are in agreement.

2. Hospice and Nursing Home Patient Liability

The Department is responsible for developing, maintaining, and following internal controls over disbursements to hospice providers and to ensure such disbursements are properly supported and appropriate for the respective services rendered in accordance with all federal reimbursable guidelines.

During the prior year's audit (fiscal year 2010) of the Department, we made recommendations to management related to payments made to providers for hospice services which included the patient cost sharing amounts. This issue was identified by the Department approximately four years ago.

During fiscal year 2011, the Department's management made significant efforts to resolve the claim processing and financial reporting aspects of the matter. During fiscal year 2011 the Department used its "Change Control Board" and "Customer Service Request" process to communicate to its claim processing vendor the need for correction. However, as of the date of this report the providers have not been billed for the overpayments since the exact amounts are not known.

During the current fiscal year audit, we noted the Department had not quantified the amount of overpayments made to hospice and nursing home providers from fiscal years 2003 through 2011. As of June 30, 2011, the exact amount of the over payments to be recovered and due to the Department were still unknown.

Based on the result of a complex calculation, the total prior years' overpayments receivable from hospice providers is expected to amount to approximately $57 million, of which approximately $39 million has been reserved as potentially uncollectible. Approximately 65 percent of amounts collected will be owed to the federal government. This will result in a net decrease in benefit expense of approximately $18 million. This audit adjustment was made by the Department.

The Department did not have appropriate and adequate safeguards in place to prevent the disbursement of overpayments to hospice and nursing home providers. This occurred because of a failure of the Division of Family and Children's Services' (DFCS) SUCCESS system to properly interface with the Medicaid Management Information System (MMIS) at the Department.

We recommend management take steps to immediately address issues that surface with systems that interface with the MMIS. Although these system issues appear to now be corrected, other such issues could arise and need prompt attention. Further, when overpayments and errors are identified, management should continue to take the time to calculate an estimate of the effect on the financial statements in the manner of the estimations performed for fiscal year 2011. Failure to estimate these amounts could cause management to be unaware of amounts owed to others or amounts owed to it that could be material. Finally, management should take steps to quantify and then seek to recover amounts owed to it by the hospice providers as soon as possible.

3. Accounts Payable and Other Accruals

The Department's management is responsible for ensuring costs associated with payment obligations are recorded promptly when incurred, and reported accurately in the financial statements as well as the schedule of expenditures of federal awards. An account payable exists when the Department has benefited from the delivery of goods or services and the related obligation remains unsatisfied.

Management of the Department provided us with a detail listing of liabilities supporting the accounts payable and other accruals reported by the Department at June 30, 2011. As a result of our audit procedures, we identified several significant obligations which were not included within the detail and thus excluded from the reported balances of the Department at year end.

An adjustment of approximately $23 million was required to properly state accounts payable and other accruals as well as the related expense.

Management within the various divisions of the Department did not provide to the Financial Services Division accurate and timely information related to accounts payable and other accruals. Additionally, appropriate understanding at the clerical level regarding the recording of accounts payable in accordance with generally accepted accounting principles (GAAP) was lacking as compared to the budget basis otherwise adopted by the Department.

In an effort to ensure the Department's reported obligations and related receivables are accurately stated, we recommend management implement a process which includes a careful review of material disbursements subsequent to year end with the intended purpose of identifying liabilities which should be reflected in the Department's accounts payable and other accruals at fiscal year end.

Additionally, we recommend the Department establish goals and provide training to employees that reinforces its accrual policies in order to ensure that liabilities are identified and recorded at the point of obligation. We recommend divisions and offices throughout the Department be charged with identifying obligations at year end, including any related liabilities, assessing those liabilities and ensuring the timely recording of those liabilities.

4. Benefits Payable at State Health Benefit Plan (SHBP) and Fiduciary Funds of the Department

The Department's management is responsible for ensuring proper administration of healthcare claims recorded in three (3) funds managed by the Department. These three (3) funds include the SHBP Fund and two (2) fiduciary funds (known as the State Employees Postemployment Health Benefit Fund (State OPEB Fund) and the School Personnel Postemployment Health Benefit Fund (School OPEB Fund)). The adoption of the accrual basis of accounting under generally accepted accounting principles is required for each of these funds.

All three (3) funds noted above include healthcare costs administered by various third party service providers. During the audit of the fiscal year June 30, 2011 and upon receipt of Department prepared financial statements, we noted a debit balance in benefits payable at the School OPEB Fund. Upon inquiry as to the nature of such a balance, it was determined that the debit balance was due to an error on the part of a third party service provider, United Healthcare (UHC), in their processing of claims paid across funds. Additionally, our inquiries resulted in noting that adjustments would be required which would affect all three (3) respective funds.

Adjustments affecting benefits payable and related accounts were required across the three (3) funds as follows: a) the SHBP Fund recognized approximately $9,929,000 to reduce benefits payable; b) the State OPEB Plan recognized approximately $4,000 to increase benefits payable; and, c) the School Personnel OPEB Fund recognized approximately $9,925,000 to increase benefits payable.

The Department should enhance communications with its third party service providers relative to all respective accounting and reporting of claims paid and expensed. Further, if discrepancies are noted by either party, then proper investigative actions should be initiated and resolved in a more timely fashion by the management of the Department.

Significant Deficiencies

5. Controls Over Processes Performed at Service Organizations (Partial Repeat of Prior Year Finding)

Management is responsible for implementing and maintaining effective internal controls over financial reporting whether the processing is performed at the Department or whether it is outsourced to an outside service organization. This responsibility includes an understanding of user controls to ensure they are implemented and maintained within the Department's internal control system.

The responsibility for user controls is not consistently communicated at the management or staff level throughout the Department. Further, designated user controls are not undergoing a thorough review process on a periodic basis to ensure they are being implemented and are effective.

In reviewing the Department's service auditor reports, management could not readily provide us information relative to the user controls that the Department has in place to detect and correct any errors that might result from improper processing. Additionally, there were issues with management's understanding of the function and purpose of user controls.

If the Department does not review and implement user controls relative to its key outsourced processes, it may be unaware of changes in the service organization's control structure that could cause transactions to be processed incorrectly. This could affect the amounts and disclosures in the financial statements.

The Department has made a conscious effort to obtain a greater understanding of the importance of reviewing the service auditor reports for significant processes and maintaining effective user controls. The Department should review the user control section in the service auditor reports on a periodic basis to ensure that they have implemented the key user controls recommended by the service organizations and that those controls are operating effectively. Additionally, the Department should communicate the importance of these controls to all appropriate levels of management and staff.

6. Verification and Documentation of Eligibility (Substantial Repeat of Prior Year Finding)

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 responsible for determining that all recipients meet prescribed eligibility requirements and those requirements are appropriately documented.

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 four (4) recipients' files in a sample of sixty (60) of Medicaid recipients whose eligibility was not properly documented. Those four (4) files included the following documentation deficiencies:

a) Two (2) case files did not contain evidence that eligibility was recertified in a timely manner in accordance with the policies and procedures in place.

b) A case file did not contain acceptable documentation of citizenship.

c) A case file was missing the application and other required documentation.

Without adherence to the Department's policies and procedures in place to determine and document Medicaid eligibility, members in the Medicaid program may no longer be eligible to receive benefits if documentation of their eligibility status is incomplete or inadequate.

An indeterminate number of participants are inadequately documented as to eligibility for Medicaid. The monetary effect is that federal funds used to fund the Medicaid program may be used to provide benefits for members who are not eligible for the program.

The Department does not have an adequate 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.

7. Matching of Allowable Expenditures
(Substantial Repeat of Prior Year Finding)

The Department is responsible for administering CHIP. CHIP is overseen by the U.S. Department of Health and Human Services through CMS. The Department is responsible for matching federal program expenditures at the federally determined rate.

The state matching rate for its CHIP expenditures is determined in accordance with the federal matching rate for such expenditures, referred to as enhanced Federal Medical Assistance Percentage (Enhanced FMAP). The Enhanced FMAP for federal fiscal year (FFY) 2011 is 75.73 percent and the Enhanced FMAP for FFY 2010 is 75.57 percent. During fieldwork, we noted twenty-five (25) instances in a sample of fifty-one (51) CHIP administrative expenditures in which incorrect federal matching rates were used. Those twenty-five (25)instances were as follows:

a) Seven (7) expenditures were incorrectly matched at the FFY 2010 Enhanced FMAP based on the date of the expenditure.

b) Eighteen (18) expenditures were incorrectly matched at a rate other than the Enhanced FMAP for CHIP expenditures.

The Department has an extensive chart of accounts to separately denote expenditure funding sources and other details. If the funding and other account information is documented incorrectly and is not corrected during the review and approval process, the expenditure could be recorded incorrectly.

The Department should improve their monitoring policy for the payment of CHIP administrative expenditures to ensure expenditures are coded appropriately and matched at the proper rate.

8. Subrecipient Monitoring For Public Health Programs (Substantial Repeat of Prior Year Finding)

The Department is responsible for administering various public health grants including the Public Health Emergency Preparedness (PHEP) program, the Ryan White Part B program, the Special Supplemental Nutrition program for Women, Infants, and Children (WIC) and the Babies Can't Wait program. These programs are overseen by various federal agencies including the U.S. Department of Health and Human Services, the U.S. Department of Agriculture, and the U.S. Department of Education. The Department is responsible for establishing and maintaining effective internal controls over compliance with the subrecipient monitoring requirements applicable to these programs.

During fieldwork, we noted two (2) instances in which the Department did not adequately establish and maintain effective internal controls over compliance with subrecipient monitoring requirements.

In the first instance, the PHEP program had initiated an agreement with the Public Health Office of Audits to monitor subrecipient compliance with program requirements for the PHEP program in March 2011. The agreement specified that each subrecipient would be reviewed once every two years. During FY 2011 a subrecipient monitoring review was conducted on only one (1) of the eighteen (18) subrecipients.

The second instance is pervasive across all public health grant programs in which awards are disbursed to the subrecipients via the Uniform Accounting System (UAS). UAS is a system in which a subrecipient district enters program expenditures for reimbursement from the Department. Each month UAS interfaces with the Department's PeopleSoft accounting software and automatically issues the subrecipient a payment based on the expenditures entered into the system. Although the payments cannot exceed the established budget amount in the PeopleSoft software, there is no Department level review of support for the expenditures for which the subrecipient is being reimbursed. As such, the UAS reimbursement process is not designed to prevent fraud or error.

The Department requires subrecipients to maintain supporting documentation for any reimbursed expenditures and requires the subrecipients to have independent audits. In addition, the Department's internal audit staff performs agreed upon procedures to review prior year expenditures for a select number of programs. However, it is endemic to the UAS reimbursement process that any review by an independent auditor or by the Department's internal audit staff occurs at a date significantly after the issuance of federal funds. As such, these reviews will not detect fraud or error in a timely manner.

The Department did not institute an adequate PHEP subrecipient monitoring process in a timely manner. As such, the Department did not have sufficient amount of time to adequately conduct the number of subrecipient monitoring reviews prescribed by the agreement in place.

In addition, the UAS reimbursement process does not prevent subrecipient noncompliance with federal program requirements and the agreed upon procedures review of prior year expenditures will not detect subrecipient noncompliance with federal program requirements in a timely manner.

The Department should put procedures in place to ensure that subrecipient monitoring reviews are conducted in a timely manner for all subrecipients. In addition, the Department should institute a process that will allow for the prevention and/or timely detection of fraud or errors related to subrecipient reimbursement via UAS.

9. Controls Over Emergency Preparedness Administrative Expenses (Substantial Repeat of Prior Year Finding SA 10-05)

The Department is responsible for administering the State of Georgia's Public Health Emergency Preparedness (PHEP) program. The PHEP program is overseen by the U.S. Department of Health and Human Services through the Centers for Disease Control and Prevention (CDC). The Department is responsible for establishing and maintaining effective internal controls over compliance with the allowable activities and cost principles applicable to the PHEP program.

The Department is required to have adequate controls to prevent and detect material errors. We noted two (2) expenditures in a sample of sixty (60) did not contain evidence of departmental approval in accordance with the procedures put in place by the Department.

The Department was unable to locate evidence to demonstrate that the expenditures were appropriately reviewed and approved as an allowable cost for the program in accordance with departmental policies and procedures.

PHEP funds may be improperly used to fund unallowable costs and activities because the policies and procedures in place at the Department to prevent and/or detect the improper payment are not being appropriately followed and/or documented.

The policies and procedures the Department has in place to prevent and detect improper usage of program funds are not functioning effectively.

The Department should improve internal controls as they relate to the review and authorization for PHEP administrative expenses.

10. Controls Over and Compliance With Control, Accountability, and Safeguarding of Vaccine

The Department is responsible for administering the State of Georgia's Immunization Grants Cluster program. The Immunization Grants Cluster program is overseen by the U.S. Department of Health and Human Services through the Centers for Disease Control and Prevention (CDC). The Department is responsible for establishing and maintaining effective internal controls over compliance with the control, accountability and safeguarding of vaccine requirements applicable to the Vaccines for Children (VFC) program.

The Department is required to have adequate controls to provide adequate oversight of providers that give vaccines under the VFC program to ensure that proper control and accountability is maintained for vaccine, vaccine is properly safeguarded, and VFC eligibility screening is conducted.

We noted six (6) provider oversight reviews in a sample of one hundred and twenty-eight (128) were not appropriately performed in accordance with the procedures put in place by the Department. The lack of the review of providers in the prescribed timeframe is a material weakness and caused material noncompliance for this compliance requirement.

Providers that give vaccines under the VFC program may not be maintaining proper control and accountability for vaccine, properly safeguarding vaccine, or conducting VFC eligibility screenings because the policies and procedures in place at the Department to oversee these providers are not being appropriately followed and/or documented.

The policies and procedures the Department has in place to oversee providers that give vaccines under the VFC program are not functioning effectively. Due to turnover, the Department did not adequately monitor the staff performing the reviews to ensure that the provider oversight reviews were performed in a timely manner.

The Department should improve internal controls as they relate to the oversight of providers that give vaccines under the VFC program. The Department should strengthen the structure of the review process to ensure that there is an individual in place to routinely monitor and document the scheduling and timely completion of the provider oversight reviews by the assigned staff. The Department should also have a written personnel succession plan in place to ensure that required functions continue to occur after personnel changes.

11. Controls Over and Compliance with Record of Immunization

The Department is responsible for administering the State of Georgia's Immunization Grants Cluster program. The Immunization Grants Cluster program is overseen by the U.S. Department of Health and Human Services through the CDC. The Department is responsible for establishing and maintaining effective internal controls over compliance with the record of immunization requirements applicable to the Vaccines for Children (VFC) program.

The Department is required to have adequate controls to provide adequate oversight of providers that give vaccines under the VFC program to ensure that a proper record of immunization is maintained for administered vaccines.

We noted six (6) provider oversight reviews in a sample of one hundred and twenty-eight (128) were not appropriately performed in accordance with the procedures put in place by the Department. The lack of the review of providers in the prescribed timeframe is a material weakness and caused material noncompliance for this compliance requirement.

Providers that give vaccines under the VFC program may not be maintaining proper records of immunization for administered vaccines because the policies and procedures in place at the Department to oversee these providers are not being appropriately followed and/or documented.

The policies and procedures the Department has in place to oversee providers that give vaccines under the VFC program are not functioning effectively. Due to turnover, the Department did not adequately monitor the staff performing the reviews to ensure that the provider oversight reviews were performed in a timely manner.

The Department should improve internal controls as they relate to the oversight of providers that give vaccines under the VFC program. The Department should strengthen the structure of the review process to ensure that there is an individual in place to routinely monitor and document the scheduling and timely completion of the provider oversight reviews by the assigned staff. The Department should also have a written personnel succession plan in place to ensure that required functions continue to occur after personnel changes.

12. Unallowable Charges to and Controls Over Ryan White Part B Expenses

The Department is responsible for administering the State of Georgia's Ryan White Part B program. The Ryan White Part B program is overseen by the U.S. Department of Health and Human Services through the HIV/AIDS Bureau of the Health Resources and Services Administration. The Department is responsible for establishing and maintaining effective internal controls over compliance with the allowable activities and cost principles applicable to the Ryan White Part B program.

The Department is required to have adequate controls to prevent and detect material errors. We noted one (1) expenditure in a sample of sixty (60) was inappropriately paid using Ryan White Part B funds due to a coding error.

One (1) expenditure in a sample of (60) was inappropriately paid using Ryan White Part B funds because there was a coding error that was not prevented or detected by the policies and procedures in place at the Department.

Ryan White Part B funds were improperly used to fund unallowable costs and activities because the policies and procedures in place at the Department to prevent and/or detect the improper payment are not functioning appropriately.

The policies and procedures the Department has in place to prevent and detect improper usage of program funds are not functioning effectively.

The Department should improve internal controls as they relate to the review and authorization of Ryan White Part B expenses.

13. Unallowable Charges to and Controls Over Babies Can't Wait Expenses

The Department is responsible for administering the State of Georgia's Babies Can't Wait program. The Babies Can't Wait program is overseen by the U.S. Department of Education. The Department is responsible for establishing and maintaining effective internal controls over compliance with the allowable activities and cost principles applicable to the Babies Can't Wait program.

The Department is required to have adequate controls to prevent and detect material errors. We noted one (1) expenditure in a sample of sixty (60) was inappropriately paid using Babies Can't Wait funds due to a coding error.

The expenditure was inappropriately paid using Babies Can't Wait funds because there was a coding error that was not prevented or detected by the policies and procedures in place at the Department.

Babies Can't Wait funds were improperly used to fund unallowable costs and activities because the policies and procedures in place at the Department to prevent and/or detect the improper payment are not functioning appropriately.

The policies and procedures the Department has in place to prevent and detect improper usage of program funds are not functioning effectively.

The Department should improve internal controls as they relate to the review and authorization of Babies Can't Wait expenses.

14. Controls Over Women, Infants, and Children (WIC) Benefit Expenses

The Department is responsible for administering the State of Georgia's WIC program. The WIC program is overseen by the U.S. Department of Agriculture. The Department is responsible for establishing and maintaining effective internal controls over compliance with the allowable activities and cost principles applicable to the WIC program.

The Department is required to have adequate controls to prevent and detect material errors. We noted one (1) expenditure in a sample of sixty (60) did not contain evidence of departmental approval in accordance with the procedures put in place by the Department.

There was no evidence one (1) expenditure in a sample of sixty (60) was appropriately reviewed and approved by program staff as an allowable cost for the program in accordance with departmental policies and procedures.

WIC funds may be improperly used to fund unallowable costs and activities because the policies and procedures in place at the Department to prevent and/or detect the improper payment are not being appropriately followed and/or documented.

The policies and procedures the Department has in place to prevent and detect improper usage of program funds are not functioning effectively.

The Department should improve internal controls as they relate to the review and authorization of WIC benefit expenses.

Management Points

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

15. Executive Level Review of Non-Routine Processes and Outsourced Activity

The Department's financial statements include a significant number of estimates which include allowances for bad debts, reserves and other accruals such as the Upper Payment Limit (UPL) estimate, estimates for claims incurred-but-not-reported (IBNR), and reserves for payments due to and from third parties. Although some of the estimates are provided to management by Department employees, many of them are performed by outside actuaries, attorneys and consultants. Additionally, Department management utilizes over twenty-five (25) third party service providers to process transactions on behalf of the Department.

Based on our observations, inquiries and other audit procedures, we have noted Department management is not currently putting sufficient focus on understanding, reviewing, and challenging the assumptions or calculations provided to them by others within the Department or outside contractors (actuaries, attorneys, and consultants) causing incorrect information to be included in the financial statements. This situation resulted in a number of significant post closing journal entries to the financial statements this year and in prior years.

Additionally, we have noted Department management has not been timely in addressing its responsibilities to perform thorough reviews of all data and information that will be included in its various operations and financial statements whether obtained from internal or external sources. Management did not appear to be proactive in addressing all issues it notes as part of its review processes. This includes: a) consideration of collectability of accounts receivable; b) safeguarding of cash; c) observations of clean cut-off in the various assets and the liabilities; and, d) the propriety of making disbursements of significant funds relative to general operations of the Department.

Department management is responsible for all output resulting from data processed by third party service providers, and should ensure that those employees who work directly with the third party service providers obtain and review reports prepared and issued by the respective third party service providers under the American Institute of Certified Public Accountants (AICPA) Statements on Standards of Attestation Engagements (SSAE) No. 16. Department management did not appear to be performing the necessary due diligence to understand the capabilities and independence of all third party service providers, validating their assumptions and carefully reviewing and challenging their work product. Proper review includes considerations of the effectiveness of the controls at those service providers and determination as to whether the recommended user controls are in place and operating effectively. Department management has a significant role to play in the assessing of the adequacy of such internal control structures and must be proactive in addressing such concerns.

We recommend Department management place priority on taking the time to thoroughly review and challenge information that is provided to them for inclusion in financial statements by both internal and external sources. We recommend the Department demonstrate a more proactive approach to addressing all of the concerns noted in the above paragraphs. The quantitative element of management in the accounting function is the demonstration that amounts balance and are supported. The qualitative element of accounting is diving into the various balances and determining their propriety and determining that all appropriate steps have been taken to turn all assets into a form of liquidity such as cash, and that all disbursements of funds are appropriate.

In conclusion, Department management should enhance its documentation to demonstrate that all of the above concerns are adequately addressed, and the quantitative and qualitative approaches to managing the accounting function are being employed. Such documentation should include:

- Copies of well-documented, reviewed and approved reconciliations of all amounts significant to the financial statements;
- Required deliverables from third parties for work performed which includes documentation of assumptions used and basis for developing the respective conclusions;
- Management’s review and acknowledgement of agreement with information provided by internal and external sources;
- Conclusions reached by management, and the basis for the respective conclusions; and,
- Concurrence of the Department’s Office of Inspector General (OIG) on matters of significance to the Department’s financial position and operations.

16. Financial Statement Preparation, Budget Comparison Reports, and Annual Closeout

During the summer of 2011, the Department created an audit report delivery time-line and schedule with assistance and agreement of the Georgia State Accounting Office (SAO), the Georgia Department of Audits and Accounts (DOAA), and the Department's annual audit engagement team. This schedule incorporated several important dates, and the schedule was shared with members of the Department's Audit Committee and the Commissioner on August 11, 2011 as well as on October 13, 2011.

Key dates noted in the schedule related to significant areas of audit such as: a) actuarial reports by September 1, 2011; b) State Health Benefit Plan (SHBP) financial statements by September 21, 2011; c) complete financial statements, notes, supplementary information, and the schedule of expenditures of federal awards (SEFA) by October 14, 2011; d) oral affirmation was to be provided to the SAO by November 11, 2011; and, all audit reports were to be issued by November 23, 2011.

The actuarial reports and the SHBP financial statements were provided at the approximate target dates; however, those reports and statements required revision by the actuaries and management due to logic errors and those revisions were not received by the audit team until October 2011. The complete financial statements, notes, supplementary information and the SEFA were several weeks in arrears. Once received in early November 2011, significant adjustments were required to further refine and adjust the financial statements and the SEFA.

To further the above thoughts, the SAO and DOAA are required to annually report on the Department of Community Health's Budget Comparison Report (BCR). All respective budgetary adjustments were scheduled to be completed and delivered to the SAO by the close of October 2011, but budgetary adjustments were recorded by management well into November 2011.

All of the above observations emphasize the need for changes to be made at the Department of Community Health relative to the accounting and financial reporting system, and the respective policies and procedures. One recommendation surrounds the need for a timelier annual closeout which will be accommodated by monthly closeouts. Another recommendation which goes beyond the monthly closeout concept is to address the need to utilize other financial reporting systems that are already provided through the SAO. This reporting system (FASTR) is set up to accommodate both budgetary and GAAP reporting. It is a web-based system and therefore data and entries could be accessed by all interested parties (DOAA, SAO and external auditors). Additionally, as the Department's data is included in the BCR and the State of Georgia's Comprehensive Annual Financial Report (CAFR) produced by SAO, it would reduce or eliminate time spent and the risks involved in having to maintain the same data in two (2) different systems. Management should contact SAO to discuss using the FASTR reporting system to produce the Department's financial statements.

17. Monthly Balancing of General Ledger Accounts

As noted in prior years as well as this current fiscal year audit, the Department takes a significant amount of time to perform the annual closeout process coupled with the Department's annual financial statement preparation process. The amount of time required to closeout and report was significantly heightened with the reorganization of the Department to include all the public and healthcare facility regulation programs of the former Department of Human Resources.

As part of our annual audit process, we noted numerous adjustments and journal entries required to be prepared, processed and recorded during the annual closeout period and deep into the audit fieldwork period. Many of the adjustments relate to matters occurring throughout the fiscal year, and not just during the final month of June.

The above observation is furthered when we audit various financial statement balance sheet accounts and note the delinquency of the balancing of accounts. The term "balancing" means taking supporting detail listings from subsidiary ledgers of financial information and reconciling such amounts to those amounts recorded on the Department's general ledger. Balancing should incorporate a requirement to resolve any differences and to make the necessary adjustments to the general ledger and, or the supporting subsidiary ledgers resulting in the ability to confidently report the statement of position and statement of operations on a monthly basis.

Currently, many of the Department's balance sheet accounts do not appear to incorporate a monthly balancing requirement. Such balance sheet accounts in which it is not apparent as to a monthly balancing include, but are not limited to: a) cash; b) Federal receivables; c) certain other receivables; d) accounts payable; and, e) deferred revenues. Other accounts such as the incurred-but-not-reported (IBNR) are estimates that stress an annual evaluation, but even those types of accounts should be periodically reviewed and adjusted accordingly, and the effect on the Federal accounts receivable is important to consider as well.

In the end, it appears much of the Department's annual closeout effort is the result of a lack of a monthly (or quarterly as determined by management) balancing of its general ledger accounts. The colossal effort at year end could be mitigated if the Department balanced its books on a monthly basis. If the Department wishes to accelerate the annual closeout process and the financial reporting preparation process, as discussed during the audit, then we believe it is imperative to require such a monthly balancing. Therefore, we recommend the Department begin monthly closeouts as part of its ongoing financial and accounting processes.

We acknowledge implementation of this suggestion will not be an easy one to accomplish as the Department is now approximately five (5) months into the current 2012 fiscal year.

However, our recommendation to kick-start this concept of monthly balancing of accounts is furthered with the following thoughts and recommendations. Effective immediately, the Department should perform a closeout and balancing of the:

- Six (6) months ending December 31, 2011;
- Three (3) months ending March 31, 2012;
- Three (3) months ending June 30, 2012;
- One (1) month ending July 31, 2012, and onward on a monthly basis.

Each of the above closeouts and process of balancing the general ledger to subsidiary ledger should be heavily scrutinized, and the demand for "getting it right" needs to be similar to the annual audit process.

The above recommendation will be a painful process to implement this first year and will require substantial effort; however, it is a process that needs to be heavily considered if the Department truly desires to "right the ship" from an accountability standpoint, and to provide for a smoother annual closeout and financial reporting process.

18. Journal Entries

The Department records a significant number of adjusting journal entries to its books and records. Management is constantly overriding the financial information system which could be construed to mean the system is not operating and working as designed, or that the users of the system need additional training and expertise in their respective areas. During our annual audit, we noted a significant number of adjusting journal entries were determined to be needed (either by management or by the audit team) to correct previously erroneously prepared, processed and recorded journal entries.

We recommend individual responsibilities be better understood and communicated within the Department, and for management to spend the appropriate time to review, scrutinize and approve adjusting journal entries. Further, we recommend more training of the Department's personnel as needed. The goal is to reduce the number of adjustments required to reverse improper or erroneous prior journal entries noted during the annual closeout and audit processes.

19. Internal Oversight Function

Department management is responsible for the quality and effectiveness of the Department's internal controls including reviewing and challenging information provided to them by internal and external sources and monitoring the controls related to financial processes. This also helps to ensure that employees perform high quality work and sets the tone for accurate financial reporting.

However, in an entity the size and complexity of the Department, even an excellent system of internal controls will only provide reasonable assurance that financial reporting errors, irregularities, fraud and operating inefficiencies will be identified, addressed and resolved. A primary method to significantly enhance the quality of internal control is to create a mechanism for additional internal oversight.

Presently, the Department's Office of the Inspector General (OIG) performs oversight in several important areas which is primarily related to operations and largely externally focused. We believe such oversight should be extended to the financial reporting arena as well. An internal oversight function would not be a substitute for management's review and monitoring. Rather, a plan would be developed for oversight personnel to conduct a series of continuous reviews in specific areas such as financial services, Medicaid and the State Health Benefit Plan which result in focused fact-based reports that include their findings and recommendations for improvement. The plan should include monitoring the satisfaction of the findings and management recommendations made each year in the annual audit. The reports generated by the internal oversight function would be reviewed with Department management and corrective action plans developed. The internal oversight function would monitor the corrective action to see that it was implemented. Such an oversight function would also provide greater confidence to everyone in the Department's management relative to financial and non-financial information generated by the system and communicated to internal and external parties. The internal oversight function should be housed in with the OIG who reports directly to the Commissioner.

20. Schedule of Expenditures of Federal Award (SEFA)

Early in the annual audit process (approximately May 2011), we discussed with Department management and the Audit Committee the need for a projected SEFA which would be the basis for the determination of the major programs for the conduct of a Single Audit, which is a compliance audit of Federal programs administered by the Department. The Department diligently calculated and projected the amounts expected to be expended under the various Federal programs which resulted in the need for five (5) major programs to be audited under the Single Audit. Throughout the months that followed, weekly audit status meetings were held with Department management and the weekly audit agenda included a question regarding the accuracy of the previously projected SEFA.

During late October through early November 2011, it was determined upon the Department's preparation of a final SEFA relative to fiscal year 2011 that significant expenditures were incurred during June 2011. In some cases, approximately 50 percent of the program spending was noted in June alone. Although management identified the June expenditures and the need to revise the SEFA, the revised SEFA was not provided in a timely manner (November 2011) which resulted in two (2) additional major programs requiring additional compliance testing.

We recommend Department management obtain and maintain a good understanding of all Federal spending, and consider the effects of such spending on the SEFA at all times. Management should be aware of what the individual programs are spending during the year to be in a better position to more timely determine which programs will be subject to a Single Audit.

21. Lack of Formal Disbursement Policies and Procedures (Substantial Repeat of 2010 Audit Management Point)

The Department's current written purchasing policies and procedures have not been updated to reflect the current policies and procedures. Many changes were needed to incorporate the Department of Public Health's (DPH) transactions on a basis consistent with other Department transactions. As a result, we noted confusion among certain Department personnel over procedures to be followed, such as when a purchase order is required and when approval from the budget department must be obtained. Failure to follow established procurement procedures could result in unauthorized expenditures or payments being made to unauthorized vendors.

In the prior year, we recommended management complete its project to formalize, in writing, the Department's purchasing and disbursement policies and procedures. As of June 30, 2011, the Department was still in the process of completing this task; however, subsequent to year end, the Department had formalized, in writing, a draft of purchasing policies and procedures as well as procurement policies and procedures.

Management should ensure the finished document is distributed to all appropriate personnel in an effort to have consistent understanding and implementation of controls over the Department's purchases. Additionally, the policies should be expanded to specifically state when a purchase order must be created. For example, it must be created no later than thirty (30) days after execution of a contract, but prior to remitting payment of the invoice.

Specific detail will eliminate any confusion or vague interpretation as to when the purchase order must be created. We recommend management expedite the completion of these documents and continue to provide training to all appropriate personnel.

22. Reconciling Bank Statements Regularly
(Partial Repeat of 2010 Audit Management Point)

During the audit, we noted the Composite State Board of Medical Examiners cash account had not been reconciled to the general ledger during the fiscal year ended June 30, 2011. The cash account is a zero balance account in which all deposits represent online credit card payments that are swept daily to other State of Georgia or Department bank and investment accounts. However, the Department reported an unreconciled balance of $219,100 in the general ledger account. The $219,100 balance is the net effect of four (4) amounts posted to the account during fiscal year 2011.

Additionally, we noted the Departments review of other bank reconciliations for other cash accounts was not always performed in a timely manner. Timely and accurate reconciliations between the monthly financial institution statements and the general ledger are important in order for errors or fraud to be detected and corrected in a timely manner as well as ensuring the Department's balances are properly reported. We recommend priority be placed on completing all bank reconciliations and adjusting the general ledger when necessary in a timely manner. Such reconciliations should be performed and reviewed monthly.

23. Accurate Reporting of Claims Receivables
(Partial Repeat of 2010 Audit Management Point)

During the audit, we noted there were receivables in the financial statements that included amounts resulting from claim errors which had been identified by a third party service provider. The detail of amounts that supported these receivables which was provided to us by management considered only the balances from claims paid during the current year plus those claims identified in the prior year that related to exact duplicates. Management was not however able to identify receivable balances relating to other claim errors identified in the prior year and recorded by management in the financial statements as of June 30, 2010, because the collection on these claim errors was not monitored during the current year.

We recommend the Department consider adopting policies and procedures to ensure receivable balances are monitored throughout the year. The procedures should include appropriate controls that allow management to monitor collection on outstanding receivables to ensure the ending receivable balance is accurately stated.

24. Accounting for Other Receivables

The Department reported certain receivables, also known as other receivables, in their draft financial statements provided to us in early November 2011. During our audit of other receivables, we noted accounts approximating $14 million which appeared to have been collected during the fiscal year ended June 30, 2011, but continued to be included in the other receivables balance. Consequently, audit adjustments were required to accurately report the amount of the Department's other receivables.

We recommend the Department's management increase its level of supervision and review of those parties responsible for accurately reconciling and recording other receivables. This effort should be performed and documented on a monthly basis along with other closing procedures.

25. SHBP Operations
(Substantial Repeat of 2010 Audit Management Point)

As part of our audit, we perform various analytical reviews of amounts reflected in the Department's annual financial statements. As part of that analysis, we noted the Department's SHBP has reported reductions in net assets (i.e., losses) for two (2) of the past three (3) fiscal years. As of June 30, 2008, the Department's SHBP reflected net assets of $473 million. As of June 30, 2011, the net assets have been reduced to a negative balance of $183 million.

Although there have been various increases noted in the contribution rates of participants and employers, the total contributions plus the State appropriations have struggled to cover the growing costs of providing healthcare to the participants. We understand management recognizes the shortfall and the reduction of assets used to satisfy claims, and have communicated their concerns to appropriate State of Georgia officials. We believe the Department should continue communicating such concerns to appropriate State of Georgia officials.

26. Inadequate Communication in the Department's Various Areas of Responsibility

During our testing of the SHBP, we noted there was inadequate communication in coordinating what members of the Department were responsible for providing certain items requested by us on the respective audit requests listing. Prior to the beginning of audit fieldwork, there was miscommunication within the Financial Management division as to who would provide certain hard copies of the respective audit requests listing which had already been prepared. As a result, we did not receive the items that had been prepared for us until the latter stages of the SHBP audit fieldwork, upon our further request.

We also noted that units did not adequately communicate with each other changes to certain inter-departmental reconciliations that were made. One example of this lack of communication is the Benefits Expense Reconciliation provided to us by the Financial Services unit. This spreadsheet is dependent on a separate reconciliation between the lag triangles and the general ledger performed by the Planning and Fiscal Analyses unit. During our audit, the Planning and Fiscal Analyses unit made changes to the calculation of the lag triangle reconciliation which had a direct effect on the Benefits Expense Reconciliation.

However, these changes were not communicated to the Financial Services unit, resulting in an inaccurate Benefits Expense Reconciliation being provided to us.

We recommend divisions adequately communicate and coordinate the provision of external audit request items which are required for the annual financial and compliance audits. Additionally, we recommend all parties within the Department adequately communicate with each other throughout the fiscal year relative to any and all changes which are important to all parties involved.

27. Write-off of Uncollectable SHBP Accounts Receivable

During our testing of Enterprise Fund receivables, we noted that approximately $4 million has been recorded as prior year uncollectable receivables from Blue Cross Blue Shield for the past three years. This amount has been fully allowed for in each of the past three years but no action has been taken by the Department to write-off of this receivable in accordance with Georgia statutes.

We recommend the Department consider turning these receivables over to the Attorney General if management has determined that they are uncollectable.

28. State Health Benefit Plan (SHBP) Documentation
(Substantial Repeat of 2010 Audit Management Point)

During our review of the SHBP claims paid during the year ended June 30, 2011, we noticed three (3) of sixty (60) claims tested did not have support for dependent eligibility. We understand the documentation supporting dependent eligibility received prior to September 2008 is stored offsite and is often difficult to locate. We believe it is important the Department have the ability to access documentation supporting eligibility 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 SHBP are scanned.

We recommend the Department continue utilizing scanning, where possible, to enable efficiency in locating documents, especially documents supporting eligibility. We further recommend the Department continue its efforts to scan documents supporting dependent eligibility which were received prior to September 2008 for all currently eligible participants in the SHBP.

29. Budgetary Approval of Purchases in the Cancer State Aid Program (CSAP) (Substantial Repeat of 2010 Audit Management Point)

During our testing of current year disbursements from the CSAP, we noted three (3) expenditures for which there was no documentation of budgetary approval, two (2) disbursements for which there was no documentation of a purchase order, two (2) disbursements for which there was no documentation of program approval and two (2) disbursements for which there was not adequate invoice support. Through discussion with Department personnel, we understand the CSAP's policy is to track all payments through an Excel spreadsheet that helps to limit purchases to only those that fall within the program's budget and that in lieu of having the budget department sign off on every purchase, the CSAP personnel meet with their budget analyst on a monthly basis to compare budget to actual expenditures.

Additionally, because transactions are approved and processed at the district level through the Uniform Accounting System (UAS) system which connects directly to the State Accounting Office, management expects the health departments to maintain their own supporting documentation for these expenditures and does not require the expenditures to be subject to the process used by the Department for its other expenditures.

The lack of consistency between the budget and program approval process in this area and other areas within the Department could lead to new employees not properly following the approval process and exceeding budget with purchases during the year. Additionally, a greater potential for error is created by not maintaining the appropriate supporting documentation.

We recommend the Department develop a uniform approval and documentation retention process, and that this process be followed by all programs and departments at the Department.

30. Violations of Purchasing Card Policy

During our fieldwork, we were not able to obtain documentation of prior approval for five (5) of the sixteen (16) purchasing card ("P-card") transactions selected for testing. For three (3) of these five (5) transactions for which prior approval could not be found, management declared that prior approval was not granted due to the urgency of these transactions. Two of these three transactions were for the order of print toner and the third transaction was for the purchase of Health Insurance Portability and Accountability Act (HIPAA) Compliance Implementation Guides.

In addition, per the P-card program policy of the Department, each Department cardholder has a single transaction limit of $2,500. During our testing of P-card transactions, six (6) of sixteen (16) transactions selected were individually over this transaction limit. Per discussion with the Department, the practice of the Department is to increase the single transaction limit with proper approval to accommodate purchasing needs. For each of the six (6) transactions referred to above, we noted that there was prior approval granted to increase the cardholder's single transaction limit above $2,500. However, this practice is in violation of the Department's current P-card Policy, which states on page 4 that "Each cardholder has a single transaction/order limit of $2,500."

During our fieldwork, we also noted another instance of noncompliance with the Department's P-card Policy: on March 13, 2011, computer equipment of $1,999 was purchased with a P-card directly through a vendor website. Per page 16 of the Department's P-card Policy, computer equipment is a prohibited purchase. Per discussion with the Department, the practice of the Department is to allow purchases of computer equipment if the purchase is made from a Statewide Contract through Team Georgia Marketplace ("TGM"), a PeopleSoft module which automatically updates the asset inventory system in PeopleSoft when purchases are made from Statewide Contracts. For this instance, the purchase was made directly through the vendor website rather than through TGM, which is a departure from the Department's practice.

We recommend that the Department clearly communicate to all P-card users the importance of obtaining prior approval for all P-card transactions. We additionally recommend that the Department maintain an audit trail of prior approval for all P-card transactions. We understand that for most transactions, documentation of prior approval is maintained electronically through the TGM module in PeopleSoft; however, there is no such documentation maintained electronically for point-of-sale transactions made directly with the vendor. All six (6) of the sixteen (16) transactions for which we could not obtain documentation of prior approval were such point-of-sale transactions. We recommend that the Department pay special regard to maintaining adequate documentation for these point-of-sale transactions.

We recommend that the Department's P-card Policy is reviewed and updated to properly document the Department's practice and to eliminate inconsistencies within the document. We understand that the Department's P-card policy must be in accordance with the Statewide P-card Policy and recognize that the Department also desires to maintain a policy which is more closely fitted to the Department's needs. Therefore, we recommend that the

Department's P-card Policy properly clarifies incongruities between the Department's policies and Statewide P-card policies which are cited in the Department's Policy.

In addition, we recommend that all parties involved in the Department's P-card program are aware of the Department's policies and procedures for P-cards. We understand that there is mandatory training for new cardholders which covers both the State P-card Policy and the Department's P-card Policy. We recommend that cardholders and approvers are made aware of the differences between the two policies and are communicated the importance of being in compliance with both Department and State P-card Policies.

31. Timely and Accurate Booking of Outstanding Items

During our audit process, we noted several significant transactions which were outstanding reconciling items for extensive periods of time, and whose disposition is considered to have been very untimely. The following outstanding reconciling items relative to the Department's cash accounts were noted as of June 30, 2011:

Cash, General Ledger Account #106010

- Outstanding deposit dated July 14, 2010 in the amount of $500,000;
- Outstanding deposit dated August 31, 2010 in the amount of $600,000;
- Outstanding disbursement dated April 6, 2011 in the amount of $900,000;
- Outstanding disbursement dated May 2, 2011 in the amount of $1,200,000;

Cash, General Ledger Account #101161

- Outstanding wire transfer disbursement dated August 24, 2010 in the amount of $20,230,715.

Also, at the time of our audit fieldwork, we noted approximately fifty (50) journal entries were required to balance the various cash accounts after the normal general ledger close. All reconciliations were approved by a member of management, yet there were still significant outstanding items which required journal entries to balance the cash accounts.

Investigating outstanding items is an important internal control procedure which mitigates the possibility that errors or irregularities can occur and not be corrected and addressed in a timely manner. Therefore, we recommend all outstanding items be investigated, addressed, corrected and adjusted in a timely manner, and not allowed to carryover for several months.

32. Adequate Review and Approval Process for Public Health Division Expenditures (Substantial Repeat of 2010 Audit Management Point)

On July 1, 2009 the Department assumed responsibility for the State of Georgia Public Health programs. As a result of that responsibility, certain expenditures of the various local health departments across the State are submitted to the Department for payment. During our testing of current year expenditures, we noted that in eleven (11) of sixty (60) expenditures chosen for testing, management did not provide adequate support for the payments. The only support available for each of the eleven (11) was a copy of the check and electronic identification of the item in the form of a screen print. All eleven (11) expenditures were expenditures submitted to the Department for payment by various health departments. Through discussions with the Department personnel, we determined that management expects the health departments to maintain their own supporting documentation for these expenditures and does not require the expenditures to be subject to the process used by the Department for its other expenditures.

We recommend that management develop formal policies and procedures for health department expenditures which would include maintaining adequate support for the expenditure, and establishing guidelines for adequate review and approval process. These guidelines should document a detailed process from start to finish for budget and program approval, and should include a description of specific forms for which approval should be documented on.

33. Authorization of Division of Public Health Federal Programs Expenditures (Partial Repeat of 2010 Audit Management Point)

Management of each of the DPH programs rely on the review and approval by knowledgeable staff to ensure that federally funded program expenditures meet federal requirements. In the prior year, we recommended management establish written guidelines delegating the authority to approve various categories of transactions for each federally funded program to specific individuals. Additionally, we recommended management communicate these program approval guidelines in writing to the Department's financial management unit.

We commend management for implementing our recommendation of communicating these program approval guidelines in writing to the Department's financial management unit. However, it was noted during our testing of the HIV program that there were still issues with allowable cost. We recommend management continue their efforts to ensure those individuals given the authority to approve various categories of transactions for each federally funded program.

34. Review of Invoices at the DPH Laboratory Program (Lab) (Substantial Repeat of 2010 Audit Management Point)

In gaining our understanding of internal controls at the Lab last year, we noted there was no periodic review of amounts posted to invoices by the Lab's medical processing software and accounting software. As noted in the prior year audit, we recommend management of the Lab periodically review invoices prior to mailing to ensure charges per the invoice are accurate for the tests performed. Additionally, there does not appear to be a review of invoices sent to counties for tests performed. To ensure invoices are sent out for all tests performed, we recommend the Department develop controls to allow for a reconciliation of invoices for tests performed. Any discrepancies should then be investigated further. We understand the Department's software currently being used by the Lab does not provide the accurate information needed to perform the reconciliations. We understand the lab is in the process of installing and implementing the use of new software that will improve the software capabilities and allow management to review invoices. We recommend management place a priority on completing the installation and implementation of the new software.

35. Verification of Revenue Received at the Lab
(Substantial Repeat of 2010 Audit Management Point)

In the prior year, during our understanding of Lab revenues, we noted the following:

- It did not appear personnel at the Lab were verifying payments received from counties to determine if they actually reflect amounts collected by counties. Counties are required to maintain documentation to verify amounts paid to the Lab agree with amounts collected by them from patients on their sliding scale fee schedule. In addition, there was no evidence of a review of this documentation performed by the Department. Currently the Lab does not have the personnel resources to be able to perform these duties.
- It did not appear personnel at the Lab were comparing the number of tests conducted during the year to total payments received to determine if revenue appears reasonable. In addition, there was no evidence of such a review being performed by the Department. Currently the software system used by the Lab does not generate reports, which shows an accurate number of tests conducted during the year. Management is in the process of installing new software that provides the ability to run reports with

accurate data. Management should make the implementation of the new software a priority in the current year.

- It did not appear revenue posted to the Department's general ledger was being reviewed to ensure it has been recorded properly. Currently, this deficiency continues to occur in the current year.

This lack of review could result in the Department receiving less than they are contractually owed or recording revenue improperly. In an effort to ensure revenue received and recorded within the general ledger is complete and accurate, we continue to recommend the Department consider implementing the following controls:

- A designated individual within the Lab should review documentation maintained at the counties on a periodic basis to ensure it supports payments received. We understand there are numerous counties so this could be performed on a rotating basis.
- A designated individual within the Lab should develop an estimate of revenue based on the number of tests conducted; this estimate should then be compared to actual revenue per the general ledger to ensure it appears reasonable. This activity could be performed monthly.
- Revenue is being recorded in the general ledger by employees who are not involved in the day to day operations of the Lab. It is recorded from the cash receipts posted to the bank account. Therefore, there is no independent verification that all revenue was posted. A designated individual at the Lab should reconcile their billings to the reports of cash receipts/revenue recorded in the general ledger on a monthly basis to ensure Lab revenues are being properly recorded.

36. Lab Receivables

(Substantial Repeat of 2010 Audit Management Point)

In the prior year, it was noted that accounts receivable at the Lab were not being recorded in the Department's general ledger. This practice continued into the current year. This occurred since the Department's management concluded, based on the dollar amount of these items in comparison to the Department's financial statements, the cost of tracking each item as a receivable would exceed the benefit. For this reason, these items flow through to the State Treasury on a cash basis. We obtained the June 30, 2011 accounts receivable aging for the infectious disease tests performed by the Lab. We also obtained the June 30, 2011 accounts receivable aging for the newborn screening receivables. The total of the two aging listings included approximately $1,900,000 in receivables that were outstanding for the Lab at year end but were not recorded in the financial statements.

We recommend that the receivables be recorded along with an allowance for doubtful accounts in the Department's financial statements.

37. Cross-Training of Employees at the Lab

(Substantial Repeat of 2010 Audit Management Point)

During our follow up procedures performed at the Lab in the current year, we continued to note key processes performed by the Director of Administrative Operations for which the Department did not have backup personnel. In the event of unexpected absences, the Department's ability to operate and report reliable financial data in a timely manner may be adversely effected.

We continue to recommend the Department examine opportunities to cross-train employees in all essential areas of operations, accounting and financial reporting. Cross-training of personnel allows for uninterrupted performance of critical functions during transition periods, emergency situations or periods of employee vacation or illness. Additionally, cross-training personnel on key processes can provide an opportunity to incorporate additional review controls which might not be currently available to management.

38. Comparison of Revenue to Expected Amounts at Vital Records (Substantial Repeat of 2010 Audit Management Point)

In a properly functioning system of internal controls, there is a periodic comparison by management of actual results to expected results, such as a budget to actual review. At Vital Records, one of the most useful comparisons to determine the reasonableness of revenue would be the number of records pulled to the revenue for these records. During prior year's audit, we noted that such a comparison was not being performed by management at Vital Records. As a result, errors in the revenue and receivable amounts reported by Vital Records, either intentional or unintentional, might not be discovered in a timely manner.

It is our understanding that management is in the process of upgrading their software, which will allow management to generate reports with the number of records pulled accurately. We commend management for taking the steps to improve their controls with the future implementation of the new software. We recommend management make the software upgrade a priority so that management can monitor revenues.

39. Daily Reconciliation to Reduce the Risk of Errors at Vital Records (Substantial Repeat of 2010 Audit Management Point)

In the prior year, it was noted that there was no daily reconciliation of orders received to payments received. In discussions with management, it is our understanding that the software system currently being used does not provide the reports needed to run this reconciliation due to the software recording all records performed, including faulty records. Vital Records installed a procedure to have an individual go into each customer's profile and record the number of records sent to the mailing office for mailing. The software cannot produce a report showing the number of records sent to the mailing office; therefore, the only way to verify the number of records produces that day would be to review each customer's profile individually. It is our understanding Vital Records is in the process of installing new software that will improve management's ability to run reports. We recommend management make the implementation of this software a priority and that the Department implement procedures for reconciling on a daily basis.

40. Women, Infants and Children (WIC) Voucher Processing (Substantial Repeat of 2010 Audit Management Point)

During our testing of Georgia's WIC, we noted the program does have interventions in place to prevent making payments on redeemed vouchers that do not have corresponding issue records. The primary intervention involves requiring local WIC service providers to batch front-end system data in which electronic files that include issue records of vouchers are transmitted daily to Georgia's WIC back-end data processor. The following information was given for the various reasons why issue records may not be available at the time of voucher presentment to Georgia's WIC Banking:

- Clinics do not batch and transmit electronic records to the back-end data processor in a timely manner;
- Voucher batches may be rejected due to mismatches in the header and footer information;
- A critical error (such as invalid voucher code) may exist; and,
- The voucher was a manual (hand written) voucher that must be mailed to the back-end data processor keying center in Indianapolis to be hand keyed into their back-end data system.

Additionally, we noted three (3) items in a sample of sixty (60) in which the amount presented for payment was in excess of the stated maximum reimbursable amount as noted within the WIC banking system. Upon review, it was determined that a claim will be paid at its face amount even if there was no corresponding issue record for the redeemed voucher.

In the three noted instances, an error was generated and payment was made for the average cost for the respective voucher code during the respective period. This actual payment was ultimately less than the maximum reimbursable amount. However, we continue to recommend management implement procedures that would prevent Georgia's WIC back-end data processor and banker from not having current issue records for active vouchers.

41. WIC Food and Nutrition Services (FNS) Program Operations (Partial Repeat of Management Point)

We noted a U.S. Department of Agriculture (USDA) FNS Federal fiscal year (FFY)-2008 Management Evaluation was conducted by the Southeast Regional Office of the FNS which identified certain findings related to the WIC program. One such finding in that report noted that "Georgia's WIC does not have a means of preventing dual participation, but the program currently detects dual participation after the fact and has intervention procedures in place developed and implemented to prevent subsequent dual participation by those participants who have previously dually enrolled."

We recommend the Department continue to work towards implementing its corrective actions in response to the USDA FNS' FFY-2008 Management Evaluation.

42. Filing of Federal Financial Reports in a Timely Manner (Partial Repeat of 2010 Audit Management Point)

During our testing of the Ryan White Part B program, we noted the SF 425 Federal Financial for Grant Number X07HA15591, was not filed within the time period required by the grant agreement. We noted the report was required to be filed by a revised submission date of July 31, 2011 but was not filed until August 1, 2011. In addition, the State funding amount was incorrect in the initially submitted report and the Department had to re-file the report.

During our testing of the Emergency Preparedness grants, we noted the SF 269 Financial Status Report for Grant Number 5U90TP417013-10, Public Health Preparedness and Response for Bioterrorism, was not filed within the time period required by the grant agreement. We noted the report was required to be filed by November 9, 2010 but was not filed until November 29, 2010.

We recommend the Department put procedures in place to ensure Federal Financial Reports are filed correctly in a timely manner.

43. Policies to Address Unallowed Costs Under Office of Management and Budget (OMB) Circular – A-87 (Substantial Repeat of 2010 Audit Management Point)

Although we did not observe any instances of the Department charging such costs to the program, the U.S. Department of Education has identified separation leave costs (addressed in OMB Circular A-87, Attachment B, paragraph 8.d.(3)), severance costs (addressed in OMB Circular A-87, Attachment B, paragraph 8.g.(3)), post retirement health benefit costs (addressed in OMB Circular A-87, Attachment B, paragraph 8.f), and costs associated with lease or rental agreements with affiliate organizations (addressed in OMB Circular A-87, Attachment B, paragraph 37.c) as potential unallowable costs that could be charged to the IDEA Part C Cluster (Babies Can't Wait) program. Management should create written policies addressing these costs and incorporate the provisions of OMB Circular A-87 to ensure these costs are only charged to the Babies Can't Wait program in accordance with OMB Circular A-87. In addition, management should communicate these written policies to the individuals who review and approve the Babies Can't Wait program expenditures.

44. Monitoring of Medicaid Administrative Expenses Processed Through the UAS (Substantial Repeat of 2010 Audit Management Point)

During our testing of Medicaid administrative expenses, we noted one (1) out of a sample of sixty (60) that were processed through the UAS, which is also utilized by the programs included under DPH to process expenses at the District Public Health Department level. However, the DPH program expenses processed through the UAS are subject to additional monitoring procedures through the Department's internal audit program. The Medicaid expenses processed through the UAS are not subjected to similar monitoring procedures. We would recommend the Department develop procedures to monitor Medicaid expenses processed through the UAS.

45. Matching of Medicaid Administrative Expenses

During our testing of Matching of Medicaid Administrative Expenses, we noted that one (1) invoice in a voucher packet containing multiple invoices did not match at the appropriate Federal Medical Assistance Percentage (FMAP). We recommend the Department improve the review process to ensure that all expenses are recorded at the appropriate FMAP.

46. Financial Reporting on Immunization Grants

During our testing of the Immunization grants, we noted the quarterly 1512 American Recovery and Reinvestment Act (ARRA) Reports for Grant Numbers 3H23IP422521-07S2 and 3U01C1000312-06S2 for the quarter ended December 31, 2010, were incorrect as they excluded December expenditures.

We recommend the Department put procedures in place to ensure Federal Financial Reports are filed correctly in a timely manner.

47. Documentation of Provider Eligibility

During our testing of provider eligibility for Medicaid, we noted certain requested documentation could not be provided by the Department. The documentation, which the Department believes it has stored electronically but has not properly indexed, included the Statement of Participation, Power of Attorney, and the Provider License. The information included on those documents was ultimately provided from other sources. We recommend the Department initiate a system to properly scan and maintain all files related to provider eligibility.

Other Matters

During our audit of the financial statements as of and for the year ended June 30, 2011, 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.

48. New GASB Standards

As has been the case for the past 10 years, the Governmental Accounting Standards Board (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. 56, Codification of Accounting and Financial Reporting Guidance Contained in AICPA Statements on Auditing Standards** which is currently effective and attempts to incorporate into GASB's literature certain accounting and financial reporting guidance that is currently included in the AICPA's Statements on Auditing Standards. Subjects include: related party transactions; subsequent events; and going concern considerations. We do not expect the Department to be affected by this statement.

b) **Statement No. 57, OPEB Measurements by Agent Employers and Agent Multiple Employer Plans** is effective the year ending June 30, 2012. This pronouncement should not affect the Department unless the Department becomes an agent for such plans.

c) **Statement No. 58, Accounting and Financial Reporting for Chapter 9 Bankruptcies.** This statement is currently effective and addresses financial reporting issues for governments who have declared bankruptcy. Therefore, we do not expect the Department to be affected by this statement.

d) **Statement No. 59, Financial Instruments Omnibus** is currently effective and deals with certain financial instruments and external investment pools. This statement is not expected to significantly affect the Department.

e) **Statement No. 60, Accounting and Financial Reporting for Service Concession Arrangements** will be effective for the Department's fiscal year ending June 30, 2013. This statement addresses arrangements where a transferor conveys to an operator the right, and related obligation, to provide public services through the use and operation of a capital asset in exchange for significant consideration.

f) **Statement No. 61, The Financial Reporting Entity: Omnibus (An Amendment to GASB No.'s 14 and 34)** is effective for the Department's fiscal year ending June 30, 2013. This standard addresses the concept and definition of a component unit. This new statement raises the bar for an entity to be included in another primary government's financial statements. This statement also addresses the recognition of joint venture arrangements with other governmental units.

g) **Statement No. 62, Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements** is effective for the Department's fiscal year ending June 30, 2013. The Financial Accounting Standards Board (FASB) has adopted a new codification and its original pronouncements are considered to be non-authoritative. This standard identifies those provisions in FASB Statements & Interpretations, APB Opinions, ARB's, and AICPA Accounting Interpretations issued before November 30, 1989 that are applicable to state and local governmental entities and incorporated into the GASB's literature. GASB Statement No. 20 is superseded by this statement. Matters of significance to the Department that are specifically addressed in this new standard include:

- Capitalization of interest costs
- Statement of net asset's classifications
- Special and extraordinary items
- Comparative financial statements
- Related party activities, transactions and relationships
- Prior period adjustments and restatements
- Accounting changes and error corrections
- Contingencies
- Extinguishment of debt
- Troubled debt restructuring
- Inventory
- Leases (capital, operating, etc.)
- Sales of real estate
- Real estate projects
- Research and development arrangements
- Broadcasters
- Cable television systems
- Insurance enterprises
- Lending activities
- Mortgage banking activities
- Regulated operations

As you can see from the above listing, there are items that are applicable and those that are not applicable to the Department.

h) **Statement No. 63, Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position** which is effective for the Department's fiscal year ending June 30, 2013.

This statement is intended to improve financial reporting by providing citizens and other users of state and local government financial reports with information about how past transactions will continue to impact a government's financial statements in the future. This statement provides a new statement of net position format to report all assets, deferred outflows of resources, liabilities, deferred inflows of resources, and net position (which is the net residual amount of the other elements). This statement requires that deferred outflows of resources and deferred inflows of resources be reported separately from assets and liabilities.

A deferred outflow of resources is a consumption of net assets that is applicable to a future reporting period. An example of a deferred outflow of resources is a government's hedging interest rate swap agreement in which the fair value becomes negative. If the hedge is determined to be effectively offsetting the changes in fair value of the debt, the decrease in the fair value of the derivative instrument would be reported as a liability with a corresponding deferred outflow of resources to reflect the fact that this decrease is not expected to be recognized in investment income in future periods.

A deferred inflow of resources is an acquisition of net assets that is applicable to a future reporting period. An example of a deferred inflow of resources is a service concession arrangement that involves a public toll road. If the government receives an up-front payment from an operator, the revenue associated with that payment will be recognized in future years because the arrangement that generated the up-front payment relates to those periods.

Statement No. 63 also amends certain provisions of Statement No. 34, Basic Financial Statements—and Management's Discussion and Analysis—for State and Local Governments, and related pronouncements to reflect the residual measure in the statement of financial position as net position, rather than net assets.

i) **Statement No. 64, Derivative Instruments: Application of Hedge Accounting Termination Provisions (An Amendment of GASB Statement No. 53)** is effective for the Department's fiscal year ending June 30, 2012. This statement is intended to improve financial reporting by state and local governments by clarifying the circumstances in which hedge accounting continues to be applied when a swap **counterparty, or a swap counterparty's credit support provider, is replaced. This** statement clarifies that when certain conditions are met, the use of hedge accounting should not be terminated. Hedge accounting entails reporting fair value changes of a hedging derivative as either deferred outflows of resources or deferred inflows of resources, rather than recognizing those changes in investment income. When a hedging derivative is terminated, Statement 53 requires that hedge accounting cease and all accumulated deferred amounts be reported in investment income.

As Statement 53 was being implemented, questions had arisen regarding situations in which a government has entered into a hedging interest rate swap or a hedging commodity swap and the swap counterparty (or the swap counterparty's credit support provider) commits or experiences an act of default or a termination event under the swap agreement through no fault of the government. When a swap counterparty (or a swap counterparty's credit support provider) is replaced through an assignment or an in-substance assignment, the GASB concluded that the government's financial position remains unchanged.

49. New GAO Yellow Book Standards

While GASB has been issuing new financial reporting pronouncements affecting governmental units, the Government Accountability Office (GAO) has been issuing revised standards relative to the audits of state and local governments. An exposure draft was issued in August 2010 by the GAO amending and revising *Government Auditing Standards* (the Yellow Book). It is expected that these standards will be finalized and issued in calendar year 2011. The more significant items addressed by the GAO in the August 2010 exposure draft included:

a) Actions required if an impairment to auditor independence is identified;

b) Definition of those charged with governance consistent with other AICPA audit guidelines;

c) Definition of internal control deficiencies to be consistent with other AICPA audit guidelines;

d) Promoting modernization of auditing standards consistent with technologies of today;

e) Added requirements for reporting restatements of previously issued financial statements;

f) Addressed standards related to 1) performance audits, and 2) internal audits; and,

g) Changed and emphasized continuing education requirements of auditors in the governmental sector to obtain a minimum of 80 hours of continuing education every two (2) years. The GAO emphasized a significant component of these hours must be directly relevant to governmental auditing. Further, audit team specialists (actuaries, engineers, etc.) have specific guidelines as well.

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.

FREE QUARTERLY CONTINUING EDUCATION AND NEWSLETTERS FOR GOVERNMENTAL CLIENTS

Free Continuing Education. **We provide free quarterly continuing education for all of our governmental clients.** Each quarter we pick a couple of significant topics tailored to be of interest to governmental entities. In an effort to accommodate our entire governmental client base, we offer the sessions several times per quarter at a variety of client provided locations resulting in greater networking among our governmental clients. We normally see approximately 100 people per quarter. We obtain the input and services of experienced outside speakers along with providing the instruction utilizing our in-house professionals. We hope Department accounting staff and officials have been able to participate in this opportunity, and that it has been beneficial to you. Examples of subjects addressed in the past few quarters include:

1. American Recovery & Reinvestment Act (ARRA) information and issues;
2. GASB updates (several sessions);
3. Internal Controls Over Revenue and Cash Receipting;
4. CAFR Preparation;
5. Collateralization of Deposits and Investments;
6. SPLOST Accounting, Reporting and Compliance;
7. Internal Controls Over Accounts Payable, Payroll and Cash Disbursements;
8. Capital Asset Accounting Processes and Controls;
9. Grant Accounting Processes and Controls;
10. American Recovery & Reinvestment Act (ARRA) Updates;
11. Policies and Procedures Manuals;
12. Segregation of Duties;
13. GASB No. 51 – Intangible Assets;
14. Single Audits for Auditees;
15. GASB No. 54 – Governmental Fund Balance (subject addressed twice);
16. Best Budgeting Practices, Policies and Processes;
17. Internal Revenue Service (IRS) Compliance Issues, Primarily Payroll Matters;
18. CAFR Preparation (2 Day Course which is scheduled next).

Governmental Newsletters. We produce newsletters tailored to meet the needs of governments. The newsletters have addressed a variety of subjects and are intended to be timely in their subject matter. The newsletters are authored by our own partners and managers, and are not purchased from an outside agency. The newsletters are produced and delivered periodically {approximately ten (10) times per year}, and are intended to keep you informed of current developments in the government finance environment.

Communication. In an effort to better communicate our free continuing education plans and newsletters, please email Lauren Payne at LPayne@mjcpa.com (send corresponding copy to medwards@mjcpa.com), and provide to her individual names, mailing addresses, email addresses and phone numbers of anyone you wish to participate and be included in our database.

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.