

REPORT BY THE
AUDITOR GENERAL
OF CALIFORNIA

**THE DEPARTMENT OF MENTAL HEALTH
HAS DEFICIENT ACCOUNTING AND GRANT
MANAGEMENT PRACTICES**



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P-364

Honorable Art Agnos, Chairman
Members, Joint Legislative
Audit Committee
State Capitol, Room 3151
Sacramento, California 95814

Dear Mr. Chairman and Members:

The Office of the Auditor General presents its report concerning the Department of Mental Health's deficient accounting and federal block grant management practices.

Respectfully submitted,

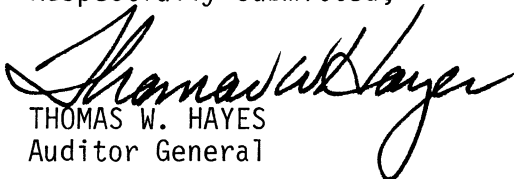

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TABLE OF CONTENTS

	<u>Page</u>
SUMMARY	i
INTRODUCTION	1
CHAPTER	
I <u>THE DEPARTMENT OF MENTAL HEALTH HAS DEFICIENT ACCOUNTING AND COLLECTION PRACTICES</u>	7
THE DEPARTMENT HAS NEITHER PROPERLY ACCOUNTED FOR NOR COLLECTED AUDIT ASSESSMENTS DUE FROM COUNTIES	7
THE DEPARTMENT HAS NOT PROMPTLY RECONCILED ITS OFFICE REVOLVING FUND	11
CONCLUSION	12
RECOMMENDATIONS	12
II <u>THE DEPARTMENT OF MENTAL HEALTH IS NOT PROPERLY MANAGING A FEDERAL BLOCK GRANT</u>	15
THE DEPARTMENT HAS WITHDRAWN FEDERAL FUNDS LONG BEFORE DISBURSING THE FUNDS	16
THE DEPARTMENT HAS NOT MAINTAINED AN ACCURATE RECORD OF COSTS OF ADMINISTERING THE ADMS BLOCK GRANT	18
THE DEPARTMENT HAS NOT AUDITED RECIPIENTS OF ADMS BLOCK GRANT FUNDS	24
CONCLUSION	25
RECOMMENDATIONS	26
RESPONSE TO THE AUDITOR GENERAL'S REPORT	
Health and Welfare Agency	29

SUMMARY

The Department of Mental Health (department) has not followed correct collection and accounting practices and has not properly managed a federal block grant. The department has failed to account for and collect audit assessments that counties owe the State and has not promptly reconciled its office revolving fund. In addition, the department has withdrawn federal block grant funds from the U.S. Treasury long before it has disbursed such funds to counties, has not maintained an accurate accounting of costs of administering the block grant, and has not audited recipients of block grant funds. As a result of these practices, the department's financial statements are inaccurate, the State and the federal government have lost potential interest income, and the department is jeopardizing continuation of funds for its largest federal grant.

Failure To Account for and Collect Money From Counties

The department has not recorded in its accounting records approximately \$39 million that counties potentially owe the State. When department auditors identify state and federal funds that counties have not spent in accordance with regulations, the auditors assess the amount that counties should remit to the State. However, the department has not recorded these audit assessments as accounts receivable, as prescribed by the State Administrative Manual, and has not collected from counties the audit assessments that are due and payable.

Of the \$39 million in audit assessments, approximately \$3 million is actually due and payable. The department has not attempted to collect this amount, even though it has the authority to offset funds that the department owes the counties. As a result, the State and the federal government have lost approximately \$160,000 in potential interest income.

Failure To Reconcile the Office Revolving Fund Promptly

The department has not performed monthly reconciliations of its office revolving fund as required by the State Administrative Manual. As of April 30, 1984, the department was unable to account for approximately \$48,000 in the fund. During our audit, the chief of the department's Accounting Section assigned an employee to reconcile the fund. As of June 30, 1984, the department had accounted for all transactions.

Failure To Manage a Federal Block Grant Properly

The department has not complied with specific funding, accounting, and auditing requirements of the federal Alcohol and Drug Abuse and Mental Health Services (ADMS) Block Grant. The department has withdrawn and held federal funds up to 242 days before disbursing the funds to counties. The department should minimize the amount of time between requesting and disbursing these funds.

In addition, during fiscal year 1983-84, the department overstated the costs of the ADMS Block Grant by approximately \$63,000. The department has also not audited recipients of federal block grant funds annually as required by federal law. As a result of these failures, the department is jeopardizing continuation of its largest federal grant program.

Recommendations

The Department of Mental Health should establish in its accounting records accounts receivable for audit assessments of counties and deduct the assessments from money that the department owes the counties. The department should also reconcile its office revolving fund monthly.

To improve its management of the ADMS Block Grant, the department should assign one person to administer the grant. Additionally, the department should implement procedures to reduce the time between withdrawing and disbursing federal funds, correctly account for costs of administering the block grant, and audit recipients of block grant funds annually.

INTRODUCTION

California law establishes a joint state-county system that provides mental health services to California residents. Counties are responsible for providing mental health services either directly in their own facilities or by contracting for the services with private agencies. The Department of Mental Health (department) is responsible for distributing state funds to counties, ensuring that counties use the funds effectively, and operating three state mental health hospitals. For fiscal year 1983-84, the State Legislature appropriated \$372 million, which the department allocated among the 58 counties for mental health services.

The amount of money allocated to a county depends on such factors as the county's population and poverty level. The department disburses monthly cash advances to each county in an amount equal to approximately one-twelfth of the county's total allocation for the year.

To receive an allocation, a county must submit to the department a spending plan that indicates the types of services it will provide and how it will provide them. State law requires that counties spend their allocations in accordance with state regulations and with the spending plans approved by the department. In addition, counties must pay at least 10 percent of the cost of the mental health services they provide.

The department has entered into a contract with the Department of Health Services whereby some of the medical services that counties provide their mental health patients are eligible for federal reimbursement under the Medi-Cal program. The Medi-Cal program is administered by the Department of Health Services. To qualify for this federal reimbursement, medical services that counties provide must conform to Medi-Cal regulations and must be provided only to mental health patients who meet Medi-Cal eligibility requirements. For fiscal year 1983-84, the contract for such Medi-Cal reimbursement was \$47 million.

At the end of each fiscal year, each county reports to the department the amount the county spent for mental health services. These reports identify separately the costs that the county claims for Medi-Cal reimbursement. The department audits the county records to determine whether the costs that the county reported could be paid with federal and state funds. If the department finds unallowable costs, it assesses the amount of state and federal funds that the county owes to the State.

A county can appeal the audit findings to the department, but the appeal must be filed within two months of receipt of the audit report or the full amount of the "audit assessment" becomes due and payable to the State. Audit assessments also become due and payable to the State when the department director issues a final decision on the appeal. The appeal process may take from 15 days to over 14 months

from the date the appeal is filed to the date the director makes a final decision. The final decision may result in the department's deducting the audit assessment from any amounts that the State may owe the county.

Federal Grants

The department manages four federal grants. For fiscal year 1983-1984, the department was awarded \$14.2 million for the federal Alcohol and Drug Abuse and Mental Health Services (ADMS) Block Grant, \$0.6 million for the Community Support System Program, \$0.3 million for the State Manpower Development Grant, and \$0.6 million for the Disaster Assistance Program.

The ADMS Block Grant provides funds to counties to operate community mental health centers, of which there are 25 in California. The community mental health centers provide out-patient services, day treatment, 24-hour emergency care, screening for admission to state institutions, and consultation and education services. The ADMS Block Grant constitutes over 90 percent of the federal grant funds that the department manages. Of the \$14.2 million in ADMS Block Grant funds received in fiscal year 1983-84, the department granted approximately \$13.2 million to counties and estimates that it will spend \$0.4 million to pay its own costs to administer the program.

The department receives the ADMS Block Grant funds through a contract with the State Department of Alcohol and Drug Programs, which is the agency responsible for all ADMS Block Grant funds received by the State. The Department of Alcohol and Drug Programs contracts with the department to manage the grant funds earmarked for mental health services.

To withdraw ADMS Block Grant funds from the U.S. Treasury, the department submits its request for funds to the Department of Alcohol and Drug Programs, which then requests the U.S. Treasury to deposit the funds immediately in a state bank account. An average of 11 days pass between the time the department submits its request and the time the funds are available for disbursement by the department.

Organization of the Department

The department carries out its responsibilities through three divisions: the Administration Division, the State Hospitals Division, and the Community Programs Division. The Administration Division, which has approximately 163 staff positions, is responsible for allocating and disbursing state and federal funds, budgeting and accounting for expenditures, and auditing county costs. The State Hospitals Division, which has its headquarters in Sacramento, has approximately 31 staff positions and is responsible for providing hospital services to mental health patients that counties refer to state hospitals. The department operates three state hospitals:

Atascadero, Metropolitan, and Patton. The Community Programs Division, which has approximately 87 staff positions, is responsible for county operations, community programs, quality assurance for mental health services, and management of federal grants. Each division contains department units, which are responsible for various functions. For fiscal year 1983-1984, the department budgeted for its own operations \$29.7 million.

The department uses the California State Accounting and Reporting Systems (CALSTARS) to account for its financial transactions. The CALSTARS is an automated accounting system available for use by state agencies. The system is capable of accounting for program costs by unit.

SCOPE AND METHODOLOGY

In this review, we evaluated the accounting system and internal controls of the Department of Mental Health for fiscal year 1983-84. We also reviewed the department's compliance with federal block grant requirements during fiscal years 1982-83 and 1983-84.

To evaluate the department's accounting system and internal controls, we reviewed pertinent requirements in the State Administrative Manual and interviewed department administrative and accounting staff to determine the department's procedures for maintaining adequate internal controls. These internal controls

include proper separation of duties, proper approval of transactions, and proper recording of transactions. After a preliminary review of all of the department's internal controls, we concentrated on the procedures for disbursements, revolving fund transactions, and collections. We selected and tested 92 transactions to determine whether they had been processed in accordance with department procedures. To calculate interest amounts on uncollected audit assessments, we used the interest rates reported by the State Treasurer for fiscal years 1982-83 and 1983-84.

To evaluate the department's compliance with federal requirements, we reviewed the department's administration of the federal Alcohol and Drug Abuse and Mental Health Services (ADMS) Block Grant since it began to administer the block grant in July 1982. We examined the Office of Management and Budget Circular A-102, "Uniform Requirements for Grants to State and Local Governments," and other federal laws and regulations pertaining to block grants. We also interviewed personnel of the U.S. Department of Health and Human Services and the U.S. Treasury. We talked to Department of Mental Health officials responsible for various aspects of grant management and accounting and reviewed the department's procedures for accounting for federal funds, requesting federal funds from the U.S. Treasury, and auditing block grant fund recipients. Finally, we selected and tested 53 transactions to determine whether the department had processed them in accordance with federal requirements.

CHAPTER I

THE DEPARTMENT OF MENTAL HEALTH HAS DEFICIENT ACCOUNTING AND COLLECTION PRACTICES

The Department of Mental Health (department) has not properly recorded as accounts receivable audit assessments totaling approximately \$39 million and has not taken sufficient action to collect them. Consequently, its financial statements are inaccurate and the State and the federal government have lost approximately \$160,000 in potential interest income. Further, because the department has not promptly reconciled its office revolving fund, it could not account for transactions totaling \$48,000.

THE DEPARTMENT HAS NEITHER PROPERLY ACCOUNTED FOR NOR COLLECTED AUDIT ASSESSMENTS DUE FROM COUNTIES

The department has not properly recorded approximately \$39 million in audit assessments resulting from audits of the counties. Moreover, it has not taken sufficient action to collect the assessments that are payable to the State. Consequently, the department's financial reports are inaccurate. Furthermore, the State and the federal government may be losing potential interest income on the uncollected amounts.

The Department Has Not
Recorded Audit Assessments
in Its Accounting Records

Section 8286 of the State Administrative Manual requires that state agencies record in their accounting records as a "contingent receivable" amounts due resulting from audits of other entities. The contingent receivable is effective on the date the entity is notified of the assessment. Any assessment that is due and payable after the appeal process is considered by the State Administrative Manual as a "valid receivable" and should be established in accounting records as an accounts receivable.

The department's legal office maintains a list of audit assessments of counties and notifies the Accounting Section when audit assessments become due and payable to the State. As of June 30, 1984, the legal office had listed audit assessments of approximately \$39 million. Approximately \$3 million of this amount was actually due and payable to the State. The Accounting Section, however, has not recorded an accounts receivable for either of these two amounts. Because the department is not complying with accounting requirements specified in the State Administrative Manual, its accounting records are misstated and the department's year-end financial statements do not accurately reflect the department's financial condition.

The chief of the department's Financial Management Branch stated that audit assessments are not established as accounts receivable in the accounting records because the State would then be required to remit to the federal government the federal share of the assessments even before the appeal process is completed. Representatives of the federal Health Care Financing Administration, however, told us that the federal government requires a state to report to the federal government the federal share of an audit assessment whether or not the state records such audit assessments in its accounting records.

The Department Has Not Collected
Audit Assessments From Counties

In addition to not recording the audit assessments as accounts receivable, the department has not taken action to collect from counties more than \$3 million in audit assessments that are due and payable. Federal funds constitute more than \$1 million of the total amount due. For example, San Francisco County has owed the State more than \$600,000 since January 1984; as of June 30, 1984, the department had not collected that audit assessment.

Section 8776.5 of the State Administrative Manual requires state agencies to establish procedures for speedy collection of amounts due from another entity. Moreover, Section 8790.1 et seq. provides procedures whereby a state agency such as the Department of Mental Health can collect amounts due from counties by deducting such amounts

from a county's monthly cash advance or from any other money that the State may owe the county.

When the department does not promptly collect amounts due from counties, the State and the federal government lose interest income that could potentially be earned on the amounts collected. The deputy director of the department's Administration Division told us that the department has not collected the \$3 million due from the counties because it also owes money to counties that had their audit assessments reduced through the appeals process. He explained that the department, in previous years, had deducted audit assessments from counties' cash advances before the appeals process was complete. Subsequently, the department owed money to some counties that received a reduction in their audit assessments through the appeals process. However, we found that, as of June 30, 1984, the department owed the counties a total of only \$1.8 million in refunds for audit assessments. Therefore, counties owed the department a balance of \$1.2 million. We estimate that the State and the federal government have lost approximately \$160,000 in potential interest income because the department did not collect the net \$1.2 million in audit assessments within 30 days after they became due and payable.

THE DEPARTMENT HAS NOT PROMPTLY
RECONCILED ITS OFFICE REVOLVING FUND

The department has not promptly reconciled its office revolving fund as required by the State Administrative Manual. As of April 30, 1984, the department could not account for transactions totaling approximately \$48,000. During our audit, the chief of the department's Accounting Section assigned someone to begin correcting this situation, and as of June 30, 1984, the department had accounted for all transactions.

Section 8100 et seq. of the State Administrative Manual allows state agencies to establish an office revolving fund to issue checks for payroll and travel advances and for other expenses when immediate payment is needed. For fiscal year 1983-1984, the department had \$300,000 in its office revolving fund.

Section 7922 of the State Administrative Manual requires agencies to reconcile their office revolving fund monthly. The unspent balance in the fund plus all payments made should equal the total amount of the revolving fund. However, we found that, as of April 30, 1984, the department had not reconciled its office revolving fund since June 1983. In June 1983, the department could not account for \$925. As of April 30, 1984, the department still had not reconciled its office revolving fund and could not account for \$48,088.

According to the chief of the Accounting Section, the department has not performed this monthly accounting procedure until recently because the chief needed her staff to perform other more important duties. During our audit, the responsibility for reconciling the office revolving fund was assigned to a new employee. As of June 30, 1984, the Accounting Section had accounted for all transactions in the office revolving fund.

CONCLUSION

The Department of Mental Health is not complying with accounting and collection requirements of the State Administrative Manual. First, it has not recorded as accounts receivable audit assessments of approximately \$39 million and has not attempted to collect \$3 million due and payable from counties. Second, it has not promptly reconciled its office revolving fund.

RECOMMENDATIONS

To comply with accounting requirements in the State Administrative Manual, the Department of Mental Health should establish in its accounting records contingent receivables and accounts receivable for audit assessments. Further, the Accounting Section should reconcile its office revolving fund every month.

To collect audit assessments that are due and payable, the department should deduct from each county's cash advances any amounts that the county owes the State in excess of refunds due the county.

CHAPTER II

THE DEPARTMENT OF MENTAL HEALTH IS NOT PROPERLY MANAGING A FEDERAL BLOCK GRANT

The Department of Mental Health is jeopardizing continuation of federal funds for the Alcohol and Drug Abuse and Mental Health Services (ADMS) Block Grant. The department has withdrawn funds from the U.S. Treasury long before disbursing the funds, has not made an accurate accounting of the costs of administering the block grant, and has not audited recipients of block grant funds. These problems occurred because of lack of communication and coordination between various units within the department. Further, the department has not assigned to any one person the responsibility to oversee the department's administration of the block grant.

The federal government provides block grant funds to states with the provision that states comply with federal laws and regulations in using the funds. Block grants, such as the ADMS Block Grant, provide money for programs in California that would otherwise have to be suspended or paid for from other sources. By law the federal government must withhold grant funds from any state that does not use those funds in accordance with federal requirements. The law further states that such funds shall be withheld until the reasons for withholding them no longer exist and there is reasonable assurance that the problem will not recur.

THE DEPARTMENT HAS WITHDRAWN
FEDERAL FUNDS LONG BEFORE
DISBURSING THE FUNDS

The federal government requires that states withdrawing ADMS Block Grant funds disburse the funds promptly. The department, however, has withdrawn block grant funds from the U.S. Treasury and kept the funds for up to 242 days before making the disbursements.

Federal law (Title 31, U.S. Code, Section 6503) and regulation (Title 31, Code of Federal Regulations, Part 205) require that states minimize the time elapsing between the withdrawal of funds from the U.S. Treasury and the disbursement of the funds. The amount withdrawn should not exceed the amount that states estimate they will immediately disburse in carrying out the purpose of the ADMS Block Grant.

To determine the maximum time that should elapse between withdrawals and disbursements, we contacted a staff member of cash management operations at the U.S. Treasury. She told us that, although there are no written recommended time limits, the general practice of most federal agencies is to limit this time to three days. For example, the U.S. Department of Agriculture has a three-day requirement for withdrawal and disbursement of federal funds for various nutrition programs.

The Department of Mental Health, however, has far exceeded this three-day period. From July 1982 through May 1984, except for one instance when the department disbursed funds on the same day it received them, the department held federal funds from 17 to 242 days before disbursing them to counties. The average time between withdrawal and disbursement was 63 days. The daily average balance of unspent federal funds during this period was \$1.8 million. We estimate that the State has earned approximately \$340,000 in interest on the unspent federal funds.

The primary reason the department had excessive amounts of unspent federal funds during fiscal year 1983-84 is that the department's County Allocation Unit scheduled withdrawals of federal funds once a quarter rather than withdrawing the funds at approximately the same time it makes disbursements. Further, the person who scheduled the quarterly withdrawals stated that he was unaware of the federal time requirements and, therefore, did not synchronize the withdrawals with the disbursements.

The chief of the department's Accounting Section told us that it would not be possible to comply with the time limits because the department has such limited control over how long it takes for the U.S. Treasury to process the withdrawal request and for the State Controller to make the disbursements. We contacted the Principal Claim Auditor at the State Controller's Division of Audits. She informed us that the claims review and payment processes may take from five to ten

days. Therefore, the department could not comply with a three-day limit. Nevertheless, the department should reduce as much as possible the number of days between withdrawals and disbursements.

THE DEPARTMENT HAS NOT MAINTAINED
AN ACCURATE RECORD OF COSTS OF
ADMINISTERING THE ADMS BLOCK GRANT

The department is not accurately accounting for its administrative costs attributable to the ADMS Block Grant. We found numerous errors in the calculation of both direct and indirect costs. We estimate that the department understated the cost of administering the ADMS Block Grant by about \$55,000 for fiscal year 1982-83. We also estimate that the department overstated accumulated costs in fiscal year 1983-84 by more than \$63,000 as of April 30, 1984.

To ensure that the department withdraws appropriate amounts of federal block grant funds from the U.S. Treasury, federal law and regulations require the department to maintain a current and accurate accounting of block grant costs. Title 45, Code of Federal Regulations, Part 96.30, states that "fiscal control and accounting procedures must be sufficient to . . . permit the tracing of funds to a level of expenditure adequate to establish that such funds have not been used in violation of the restrictions and prohibitions of the statute authorizing the block grant."

Federal guidelines permit the department to charge two types of costs to federal grant programs: direct costs and indirect costs. Direct costs, according to the Federal Management Circular 74-4, are costs directly related to the administration of the grant. Direct costs include the salaries and benefits of persons who work directly in administering the grant. Indirect costs are costs that the department incurs for general purposes not attributable to any one program. Indirect costs are computed as a percentage of the direct costs. The percentage, or "indirect cost rate," is determined annually by the department and approved by the Department of Finance and the federal agency involved.

The department's Accounting Section maintains special accounts in the California State Accounting and Reporting Systems (CALSTARS) to accumulate the direct and indirect costs for the administration of the ADMS Block Grant. The department charges the block grant accounts for these costs by two methods: by direct charge or by time allocation report. The department uses the direct charge method to record costs for employees who hold positions authorized for administering the ADMS Block Grant. The department's Accounting Section receives notification of such employees and enters their salaries and benefits (direct costs) into the CALSTARS. The CALSTARS automatically calculates the indirect costs for these employees.

The department uses the time allocation report method to charge for employees who do not hold positions authorized for

administering the ADMS Block Grant and who spend only a percentage of their time on the block grant. Supervisors report to the Accounting Section the percent of time that such employees work on the block grant. The Accounting Section calculates the direct and indirect costs to charge for such employees and enters these costs into the CALSTARS.

For fiscal years 1982-83 and 1983-84, the department had 9.5 positions authorized for the ADMS Block Grant. However, during fiscal year 1982-83, only 1.5 of these positions were filled. The department used the direct charge method to charge the block grant for these 1.5 positions and used the time allocation report method to charge for other people who worked on the block grant. Conversely, in fiscal year 1983-84, 7.5 of the authorized positions were filled; the department used the direct charge method to charge for these positions.

The Department Has Charged Inaccurate Direct Costs

We found errors in the time allocation report of one of the five department units that reported salary costs attributable to the ADMS Block Grant in fiscal year 1982-83; this unit failed to report salary costs of employees who had worked for five months on the block grant. Because of the unit's error, the department understated direct costs by \$30,732 in fiscal year 1982-83. As a result of this error, along with other errors in calculating salary and benefits, the department understated the direct costs for salaries and benefits in fiscal year 1982-83 by a total of \$35,000.

We interviewed the unit supervisor to determine why the unit's time allocation report was not accurate. The supervisor said that he did not report salary costs for the five months because he did not know that the time allocation reports were to be submitted for each pay period.

We also found errors in the department's calculations of direct costs for fiscal year 1983-84. We found instances where units were charging full-time positions to the ADMS Block Grant for employees who were not working on the grant full time. For example, we found that one unit charged the block grant for 100 percent of an employee's time for a ten-month period. The employee told us he had worked only 50 percent of the time on the block grant for a seven-month period. This one error resulted in overstated direct cost of about \$29,000. This error, along with other errors in calculating salary and benefits, resulted in overstating the direct costs for salaries and benefits in fiscal year 1983-84 by \$44,000.

We interviewed two unit supervisors to determine why these direct charges were incorrect. One unit supervisor said that he was not aware that his employee's salary and benefits were being charged to the block grant. The second supervisor claimed that it is difficult to revise the amount charged for an employee who worked less than full time in a position that is authorized full time for the block grant.

The Department Has Charged
Incorrect Indirect Costs

We also found errors in the department's calculations of indirect costs. According to the Federal Management Circular 74-4, the department should determine indirect costs by multiplying the direct costs for salaries and benefits by the "indirect cost rate." The indirect cost rate is a percentage of the direct costs. The department computes this rate annually and submits it to the Department of Finance and to the federal government for approval. In fiscal year 1982-83, the department's approved indirect cost rate was 53.7 percent. For fiscal year 1983-84, the approved indirect cost rate was 42.3 percent.

For fiscal year 1982-83, the chief of the Accounting Section made two errors in calculating indirect costs that almost offset each other. First, the chief incorrectly computed the direct costs for the year by inadvertently adding \$29,315 to the direct costs. The chief then applied the indirect cost rate to the incorrect figure for direct costs which resulted in overstating the indirect costs. Second, the chief used an indirect cost rate of 29.49 percent instead of the approved rate of 53.7 percent; this error resulted in understating indirect costs by \$30,612. As the net result of these errors, the department charged the grant program \$1,297 less than it should have.

The chief of the Accounting Section stated that she obtained the indirect cost rate of 29.49 percent from the department's Budget Section. However, she has no record of this instruction from the

Budget Section. Further, obtaining the indirect cost rate from the Budget Section is contrary to established department procedures that direct department staff to obtain the indirect cost rate from the Fiscal Analysis Section, which has been under the supervision of the chief of the Accounting Section since October 1983.

At present, no person reviews the chief's calculation of the costs. The chief of the Accounting Section has 23 subordinates in her section. In our opinion, the accuracy of such calculations would be improved if the chief would delegate these calculations to one of her subordinates and then review the subordinate's calculations.

We also found that the department used wrong indirect cost rates in the CALSTARS in fiscal year 1983-84. The indirect cost rates that the department used ranged from 36 to 84 percent even though the approved rate was 42.3 percent. The CALSTARS consultant at the Department of Finance told us that the chief of the Accounting Section can change the indirect cost rate used in the CALSTARS.

As a result of the inaccurate direct and indirect costs charged to the ADMS Block Grant, the department does not have accurate, up-to-date financial reports. Therefore, managers do not know the current cost of the program or how much money may be available for additional administrative expenditures. Further, if the errors continue and they become substantial, the department may withdraw insufficient federal funds and thus have to pay costs of the ADMS Block Grant from other funds.

THE DEPARTMENT HAS NOT AUDITED
RECIPIENTS OF ADMS BLOCK GRANT FUNDS

The department has not audited recipients of ADMS Block Grant funds and does not plan to audit the recipients annually as required by federal law. Instead, the department plans to perform the audit every two years. As of May 1984, the department had disbursed \$21 million in ADMS Block Grant funds to 25 recipients. Because the department has not audited recipients of block grant funds, it lacks assurance that recipients have spent the \$21 million for authorized purposes.

Federal law requires annual audits of recipients of ADMS Block Grant funds. Title XIX of the Public Health Services Act, Section 1916(b)(2), requires the State to audit expenditures of the ADMS Block Grant funds annually. In addition, the 1983 Catalog of Federal Domestic Assistance, issued by the U.S. Office of Management and Budget, specified that each state must annually audit its expenditures under the ADMS Block Grant.

However, the chief of the department's Audit Section stated that he plans to audit recipients of ADMS Block Grant funds only once every two years. He states that biennial audits are acceptable under the Office of Management and Budgets Circular A-102, which states that audits will usually be made annually but not less frequently than every two years. However, personnel of the Division of Grants and Contracts Management at the Alcohol, Drug Abuse and Mental Health Administration of the U.S. Department of Health and Human Services told us that whenever federal requirements conflict, federal law takes precedence.

Department memos and records reflect confusion on the audit requirement. In its "Proposal for the State Assumption of the Block Grant," the department stated that the audit of recipients of block grant funds would be performed annually as required by federal law. Two department memos, however, issued in February 1983, gave conflicting due dates for audits. The chief of the department's Statewide Mental Health Planning Section stated that the audit was due in January 1984, whereas the chief of the Planning, Evaluation and Promotion Division stated that audits were required by July 1983. In June 1984, the Audit Section began an audit of an ADMS Block Grant recipient to determine the personnel and time that such an audit would require. Audits of other recipients of ADMS Block Grant funds are to begin in October 1984.

The department has not assigned a single person as manager of the ADMS Block Grant. Assigning one person to manage the grant could resolve such conflicts regarding the date and frequency of the audits.

CONCLUSION

We found several areas where the Department of Mental Health has not administered the ADMS Block Grant in accordance with the federal laws and regulations. First, the department does not minimize the time between withdrawing block grant funds from the U.S. Treasury and disbursing the funds. In fact, the department has held U.S. Treasury funds for an average of 63

days. This average greatly exceeds the time within which the department should withdraw and disburse the funds. Second, the department has not provided current and accurate financial records of costs of administering the block grant. Federal regulations require the department to account for these funds accurately. Third, the department has not audited recipients of ADMS Block Grant funds in the two years that it has administered this block grant. Federal law requires annual audits. Because the department has failed to administer the ADMS Block Grant in accordance with federal laws and regulations, it is jeopardizing the continuance of federal block grant funds.

RECOMMENDATIONS

To comply with federal requirements for the administration of the ADMS Block Grant and to provide proper management of the ADMS Block Grant, the Department of Mental Health should do the following:

- Place the administration of the ADMS Block Grant under one person who has sufficient authority to ensure that federal requirements are being met;
- Immediately implement procedures for withdrawing money from the U.S. Treasury and making disbursements to

recipients so that the time between these two actions is minimized. The chief of the department's Accounting Section should coordinate the withdrawal and disbursement functions within the Accounting Section; and

- Direct the Audit Section to revise current policy and audit recipients of ADMS Block Grant funds annually.


To comply with the federal grant requirements and to ensure that the department maintains current and accurate accounting records for the ADMS Block Grant, the department should do the following:

- Restrict the use of authorized ADMS Block Grant positions to persons who work on the block grant full time. Use time allocation reports for persons who work on the ADMS Block Grant for less than full time;
- Instruct department supervisors on the proper methods for completing the time allocation reports and on the importance of completing the reports accurately;
- Implement accounting practices for entering direct and indirect costs correctly into the ADMS Block Grant accounts on a monthly basis. These practices should include correct monthly and year-to-date entries; and

- Direct the chief of the Accounting Section to delegate to subordinates the responsibility of calculating the direct and indirect costs, and entering the costs into the CALSTARS. The chief should review the subordinates' work for accuracy.

We conducted this review under the authority vested in the Auditor General by Section 10500 et seq. of the California Government Code and according to generally accepted governmental auditing standards. We limited our review to those areas specified in the audit scope section of this report.

Respectfully submitted,


THOMAS W. HAYES
Auditor General

Date: August 27, 1984

Staff: Steven L. Schutte, Audit Manager
Enrique G. Farias, CPA
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HEALTH and WELFARE AGENCY
OFFICE OF THE SECRETARY
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August 23, 1984

Thomas W. Hayes
Auditor General
State of California
660 J Street, Suite 300
Sacramento, CA 95814

Dear Mr. Hayes:

AUDITOR GENERAL'S REPORT, P-364

We have reviewed Report P-364, "Report by the Office of the Auditor General to the Joint Legislative Audit Committee", August 1984, and have the following comments:

1. Recommendation: "To comply with accounting requirements in the State Administrative Manual, the Department of Mental Health should establish in its accounting records contingent receivables and accounts receivable for audit assessments. Further, the Accounting Section should reconcile its office revolving fund every month."

Response: We agree in concept that the Department should establish contingent receivables and accounts receivable for audit assessments in our accounting records. Practically speaking, however, it is untenable for the State to make offsets to recover funds owed the State while the State owes other funds, often in greater amounts, to the counties but can't pay them immediately due to the time consuming Board of Control and legislative appropriation processes. For this reason it has been the Department's policy not to establish audit assessment accounts receivable. *

We agree that the Accounting Section should reconcile its office revolving fund every month. We expect to accomplish the necessary monthly reconciliation. Top priority will be given to this activity.

*Auditor General Comment: By not recording an accounts receivable for the audit assessments, the department is not in compliance with the accounting requirements specified in the State Administrative Manual. Consequently, as pointed out on page 8 of our report, the department's accounting records are misstated and its year-end financial statements do not accurately reflect the department's financial condition.

2. Recommendation: "To collect audit assessments that are due and payable, the Department should deduct from each county's cash advances any amounts that the county owes the State in excess of refunds due the county."

Response: Agree. The Department plans to initiate this action.

3. Recommendation: "Place the administration of the ADMS Block Grant under one person who has sufficient authority to ensure that federal requirements are being met."

Response: Agree. This responsibility has been delegated to the Division of Community Programs. The Deputy Director of the Division of Community Programs has assigned a single staff member to perform the total administrative function.

4. Recommendation: "Immediately implement procedures for withdrawing money from the U.S. Treasury and making disbursements to recipients so that the time between these two actions is minimized. The Chief of the Department's Accounting Section should coordinate the withdrawal and disbursement functions within the Accounting Section."

Response: Agree. The time between withdrawal and disbursement should be minimized. It will be the responsibility of the person designated within the Division of Community Programs to oversee this function and coordinate with the Department's Accounting Section regarding withdrawals and disbursements.

5. Recommendation: "Direct the Audit Section to revise current policy and audit recipients of ADMS Block Grant funds annually."

Response: The Department will review its policy regarding audits of block grant recipients and will comply with federal statutes. A high priority will be placed on meeting this commitment.

6. Recommendation: "Restrict the use of authorized ADMS Block Grant positions to persons who work on the block grant full time. Use time allocations reports for persons who work on the ADMS Block Grant for less than full time."

Response: Agree. The Department is currently conducting a study to determine which Department staff should be assigned to this activity on a full time basis. Any other staff who devote less than full time to block grant work will report on monthly time allocation records.

7. Recommendation: "Instruct Department supervisors on the proper methods for completing the time allocation reports and on the importance of completing the reports accurately."

Response: Agree. The Department will develop and implement a time reporting procedure. Division of Community Programs staff will have responsibility for this activity.

8. Recommendation: "Implement accounting practices for entering direct and indirect costs correctly into the ADMS Block Grant accounts on a monthly basis. These practices should include correct monthly and year-to-date entries."

Response: Agree. To preclude additional costs, however, implementation must be accomplished on a manual basis.

9. Recommendation: "Direct the Chief of the Accounting Section to delegate to subordinates the responsibility of calculating the direct and indirect costs, and entering the costs into the CALSTARS. The chief should review the subordinates' work for accuracy."

Response: Agree. The Department will comply with this recommendation.

If you have any questions, please contact Douglas G. Arnold, Deputy Director, Administration Division (916) 323-8261.

Sincerely,


DAVID B. SWOAP
Secretary

cc: D. Michael O'Connor, M.D.
Director
Department of Mental Health

cc: Members of the Legislature
Office of the Governor
Office of the Lieutenant Governor
State Controller
Legislative Analyst
Assembly Office of Research
Senate Office of Research
Assembly Majority/Minority Consultants
Senate Majority/Minority Consultants
Capitol Press Corps