Information Technology Division

Findings on Compliance with Rules and Regulations

Finding Number 70: $1,533,262 in Additional Costs Included in the 1997 Rates Effecting Both Federal and State Programs
The Information Technology Division had $1,533,262 in additional costs in computing its final 1997 rates, which were prepared in fiscal year 1998. These costs effected the rates that were charged to both federal and state programs.

Costs as shown in MMARS and allocable to the Information Technology Division (Division) in accordance with OMB Circular A-87, *Cost Principles for State, Local and Indian Tribal Governments*, were used as a basis for preparing final rates for 1997 telecommunications, mail and computer services. During the audit of the rates the following was noted.

- A credit of $1,285 from retirement board was not netted against expenditures. This affected all rates. During the preparation of the 1998 rates, this amount was added as expenditure, not subtracted. As a result, the amount that should now be credited is $2,570.

- Salaries totaling $15,551 and related fringe benefits of $4,510 were not included. This resulted in an under recovery of $20,061 for all rates. Only the $15,551 was deducted in the 1998 final rates. An under recovery of $4,510 remains.

- Revenue of $1,535,202 received from the telephone company for overcharges was not credited against telecommunications expenditures. The Division has stated that the credits will be processed in fiscal year 2000.

The omission of fringe benefits and netting of retirement board revenue against expenditures was an oversight. The telephone credits will be processed once the Legislature approves the fiscal 2000 budget.

The cost of mail, computer services and telecommunications, which comprised 9%, 90% and 1%, respectively of total Division costs, all had net cost under recoveries of $920,475, $9,332,840 and $108,094, respectively.

The net remaining over recovery for fiscal year 1997 was $1,533,262 (-$2,570+$4,510-$1,535,202.) Of that amount, the net credit of $1,940 (-$2,570+$4,510) due to adding the revenue from retirement board as an expenditure and omitting fringe benefits, related to developing all rates. The remaining over recovery of $1,535,202 related solely to telecommunications. These over recoveries represented 5% of the total costs of the Division.

In order to assess the effect of the net $1,940 under recovery remaining to each type of service, the under recovery was allocated according to the percentage each service was to total Division costs. It is estimated that there would be a net under recovery of $920,300 ($920,475 - $1,940 X 9%) for mail, $9,331,094 ($9,332,840 - $1,940 X 90%) for computer usage and $108,075 ($108,094 - $1,940 X1%) for telecommunications. The amount of costs that should have been billed to individual users could not readily be determined.

The estimated telecommunications under recovery of $108,075 would become an over recovery of $1,427,127 by netting the revenue of $1,535,202 received against expenditures ($108,075-$1,535,202.) The exact impact on federal programs could not be readily determined.

During fiscal year 1999, the Division adjusted the 1998 final rates to reflect the $895,032 ($335032 and $560,000) in over recoveries in the final 1996 rates and the $1,397,990 ($1,413,541-$15,551) in over recoveries in the final 1997 rates. The error in computing the wide-area network was also adjusted. (*Unknown Federal Programs; Fiscal Year 1998 Single Audit Finding 67*)

Recommendation
The Information Technology Division should adjust future billing rates for the under charges and credit departments with the telecommunications overcharges.

Department Corrective Action Plan
SINGLE AUDITOR STATED: A credit of $1,285 from retirement board was not netted against expenditures. This affected all rates. During the preparation of the 1998 rates, this amount was added as expenditure, not subtracted. As a result, the amount that should now be credited is $2,570.

Salaries totaling $15,551 and related fringe benefits of $4,510 were not included. This resulted in an under recovery of $20,061 for all rates. Only the $15,551 was deducted in the 1998 final rates. An under recovery of $4,510 remains.

ITD AGREES WITH THE SINGLE AUDITOR: A credit for $2,570 and a debit for $4,510 will be included in the reconciliation for FY2000.

SINGLE AUDITOR STATED: Revenue of $1,535,202 received from the telephone company for overcharges was not credited against telecommunications expenditures. The Division has stated that the credits will be processed in fiscal year 2000.

ITD partially AGREES WITH THE SINGLE AUDITOR: ITD processed the credits in fiscal year 2000. It should be noted that the amount is negative expense that was incorrectly posted as revenue. The ITD Cost Allocation Plan allocates expenditures for a fiscal year.

In addition, federal officials and the Single Auditor require that ITD bill (exchange money as oppose to memo or imputed billing) over or under reconciled amounts to those client agencies that paid ITD through out the year with federal funds (MMARS code 100 and 900). There is no justification for this in A-87, ASMB C-10 or 45 CFR 95 Subpart F. The justification from a federal official of the US Department of Health and Human Services, Division of Cost Allocation, was that he wants an audit trail through MMARS because MMARS cannot account for "non-cash billings". ITD's budget should not be a "way station" for federal auditors. In prior years it was not an issue because the net amounts were small and our IV revenue covered the over or under billings. This year our budget was impacted by $200,000 based on $2 million of expense refunds from the telephone vendors. That is, $1.5 million from fiscal year 97 and $0.5 million from fiscal year 1998. ITD will not comply with this directive in the future and ITD will seek to recover the $200,000.

Responsible Individual: David Lewis

Findings on Compliance with Rules and Regulations

Finding Number 71: Documentation Supporting Rate Development Needs Improvement
The Information Technology Division did not include all required documentation in developing its 1998 rates.

The Information Technology Division (Division) is responsible for preparing rates used to directly bill Commonwealth departments for mail, computer, and telecommunications services.

OMB Circular A-87 (Circular) and ASMB C-10 *Cost Principles and Procedures for Developing Cost Allocation Plans and Indirect Cost Rates for Agreements with the Federal Government*, the implementation guide (Guide) for Circular A-87, specifies certain minimum documentation that must be prepared for billed services, when the services are billed to federal awards. During a review of the 1998 final rates, it was noted that certain aspects of the Division's rate documentation were not in compliance with the Circular and the Guide.

The Division did not prepare all documentation that is required for billed services rate development. Sections 4.5.1, 4.5.2 and 4.7 of the Guide outlines certain minimum documentation that must be prepared for billed services. The following information was not provided as follows:

- An organization chart showing detail as to whether an organization is considered administrative and which certain organizations it benefits or whether it provides a service(s) and which service(s) it provides. An organization chart was provided but the detail concerning each organization was not included;

- A copy of the comprehensive annual financial report (CAFR) or information, which reconciles to the CAFR, to support allowable costs of each activity. Upon request, the Division subsequently performed a reconciliation of the costs to MMARS;

- A certification that the plan was prepared in accordance with Circular A-87, it contains only allowable costs and was prepared in a manner that treated similar costs consistently among the various federal awards and between federal and nonfederal awards/activities;

- A written narrative description of each service billed. Some services are included in a document entitled *Additional Documentation for Fiscal Years 1988 to Present.* None of the new or changed services, such as the warehouse and telecommunications, are described;

- A written narrative of the methodology used to charge the costs of each service to users, including how billing rates were determined. None of the new or changed services are described;

- A written narrative on how any variances will be handled; and

- A reconciliation of retained earnings for each type of service, i.e., computer, mail and telecommunications.

As noted above, there was a significant change in the manner in which telecommunications charges were billed in 1997 and 1998. The telecommunications system was out-sourced, thereby reducing the cost of that service from 28% of the Division's costs in 1996 to 1% in 1997 and less than 1% in 1998. The Plan currently in effect does not describe the change in methodology. Also, a new data warehousing service has been added. The 1983 agreement with the US Department of Health and Human Services (HHS) notes that any change in methodology must be submitted to HHS for review and approval. The exact impact on federal programs could not be readily determined.

During the fiscal year, the Division reached an agreement with the HHS, Division of Cost Allocation that computer equipment could be depreciated using a $25,000 capitalization policy, which is in accordance with Title 45 Code of Federal Regulations Part 95. This agreement was reached as a portion of the equipment used benefits public assistance agencies. The remaining Division equipment would be depreciated using the $5,000 as required by the Circular. In addition, the time keeping system was reviewed and certain positions, which work in multiple cost centers, are required to track their time to support the allocation of the time between services provided. Those that work in one cost center can provide an annual certificate as described in Circular A-87, Attachment B Section 11 h, to support their time. (*Unknown Federal Programs; Fiscal Year 1998 Single Audit Finding 68*)

Recommendation
The Information Technology Division should ensure that the documentation supporting future rates is in compliance with the minimum requirements as stated in OMB Circular A-87, *Cost Principles for State, Local and Indian Tribal Governments and ASMB C-10 Cost Principles and Procedures for Developing Cost Allocation Plans and Indirect Cost Rates for Agreements with the Federal Government.* In addition, the new methodology, should be submitted for approval to the US Department of Health and Human Services.

Department Corrective Action Plan
SINGLE AUDITOR STATED: An organization chart was provided but the detail concerning each organization was not included;

ITD DISAGREES WITH THE SINGLE AUDITOR: ITD provided an organization chart that complies with Circular A-87 (Attachment C Part E. "Documentation Requirements for Submitted Plans") and ASMB C-10.

The organization chart contained sufficient information to understand the ITD organization to the level specified by Circular A-87. The organization chart corresponded to the financial statements and worksheets provided to the auditor.

SINGLE AUDITOR STATED: A copy of the comprehensive annual financial report (CAFR) or information, which reconciles to the CAFR, to support allowable costs of each activity. Upon request, the Division subsequently performed a reconciliation of the costs to MMARS;

ITD AGREES WITH THE SINGLE AUDITOR: ITD typically provides this schedule. Not providing it was an oversight.

SINGLE AUDITOR STATED: A certification that the plan was prepared in accordance with Circular A-87, it contains only allowable costs and was prepared in a manner that treated similar costs consistently among the various federal awards and between federal and nonfederal awards/activities;

ITD AGREES WITH THE SINGLE AUDITOR: The form in OMB A-87 will be copied and signed by the CFO of ITD.

SINGLE AUDITOR STATED: A written narrative description of each service billed. Some services are included in a document entitled "Additional Documentation for Fiscal Years 1988 to Present." None of the new or changed services, such as the warehouse and telecommunications, are described;

ITD AGREES WITH THE SINGLE AUDITOR: ITD provides many services to its customers. Two relatively new services were not included in the description of service narrative. It should be noted that these services are usage based. The allocation base for charging out the Information Warehouse is the similar to the allocation base used charge out the MMARS system. The telecommunications costs are allocated based on the amounts billed by the CNSA contract telephone vendors (Bell Atlantic and

MCI) to each state agency.

SINGLE AUDITOR STATED: A written narrative of the methodology used to charge the costs of each service to users, including how billing rates were determined. None of the new or changed services are described;

ITD AGREES WITH THE SINGLE AUDITOR: ITD provides many services to its customers. Two relatively new services were not included in the description of service narrative.

SINGLE AUDITOR STATED: A written narrative on how any variances will be handled; and

ITD DISAGREES WITH THE SINGLE AUDITOR: This is clearly detailed in the ITD cost allocation plan. ITD bills its clients 12 monthly "estimates" (as defined by Circular A-87) during the fiscal year and after December 31 of the following fiscal year it reconciles the monthly "estimated" billings to the actual costs of the agency. Rollovers and adjustments comply with Circular A-87 Attachment C G-4.

> 4. Adjustments of billed central services. Billing rates used to charge Federal awards shall be based on the estimated costs of providing the services, including an estimate of the allocable central service costs. A comparison of the revenue generated by each billed service (including total revenues whether or not billed or collected) to the actual allowable costs of the service will be made at least annually, and an adjustment will be made for the difference between the revenue and the allowable costs. These adjustments will be made through one of the following adjustment methods: (a) a cash refund to the Federal Government for the Federal share of the adjustment, (b) credits to the amounts charged to the individual programs, (c) adjustments to future billing rates, or (d) adjustments to allocated central service costs. Adjustments to allocated central services will not be permitted where the total amount of the adjustment for a particular service (Federal share and non-Federal) share exceeds $500,000. [Circular A-87 Attachment C G-4]

SINGLE AUDITOR STATED: A reconciliation of retained earnings for each type of service, i.e., computer, mail and telecommunications.

ITD DISAGREES WITH THE SINGLE AUDITOR: US Department of Health and Human Services officials were not sure if ITD was an OMB Circular A-87 Attachment C type of organization or an OMB Circular A-87 Attachment D type of organization. An A-87 Attachment D type of organization does not require a reconciliation of retained earnings statement. Federal officials did not require the reconciliation until the issue was clarified. The issue was clarified after the auditors finished their audit.

SINGLE AUDITOR STATED: In addition, the new methodology, should be submitted for approval to the US Department of Health and Human Services.

ITD AGREES WITH THE SINGLE AUDITOR: The last time ITD submitted documents to the New York regional office of the Division of Cost Allocation, ITD was met with remarks that were not solicitous.

ITD will submit these documents again.

Responsible Individual: David Lewis

Findings on Compliance with Rules and Regulations

Finding Number 72: Internal Controls over Rate Preparation Need Improvement
The Information Technology Division needs to improve internal control over the preparation of final rates that were charged to both federal and state programs

Costs as shown in MMARS and allocable to the Information Technology Division (Division) in accordance with OMB Circular A-87, *Cost Principles for State, Local and Indian Tribal Governments*, were used as a basis for preparing final rates for 1998 telecommunications, mail and computer services. During the audit of the rates the following was noted.

- An amount of $552,650, which the Division reimbursed the general fund for fringe benefits, was not deducted before adding the federally approved fringe benefit rate of 29%. This resulted in an $552,650 over recovery on all rates.
- The amount included for lease purchases was understated by $1,209,642 resulting in an under recovery on all rates.
- The salary of one individual was added in twice resulting in an $70,269 over charge on the network.
- The amounts deducted for capital equipment and added for depreciation were from the 1997 final rates. This resulted in a net $842,914 under recovery which applied to all rates.
- The amounts deducted for equipment use allowance were from the 1997 final rates. This resulted in an over recovery of $41,491 applicable to all rates.
- Commonwealth received approval of the 1998 SWCAP after the 1998 rates were prepared. As a result, the amounts used in the rates for the executive office allocation was understated by $1,556,578 and the state-wide cost allocation plan (SWCAP) amount was overstated by $10,765. An additional amount of $1,545,813 can be added as an under recovery for 1998.

- The rate used to compute space use was $16.67/square foot, which was the rate in the previously approved SWCAP. The rate subsequently approved in the SWCAP was $15.02. This resulted in a $28,958 over recovery on all rates.

Total Division costs before adjustment for the items noted above was $30,294,413. Revenue as recorded in MMARS was $11,022,416 for a net under recovery of $19,271,997. The net over/under recovery by service could not readily be determined.

The Division stated that the miscalculations were an oversight and that it was not aware that the 1998 SWCAP was approved after the rates were prepared. The Division does not have a detail step-by-step methodology, which would serve as a checklist to ensure all items are included or adjusted. (*Unknown Federal Programs*)

Recommendation
The Information Technology Division should review the 1998 rates and adjust future rates for any variances. In addition, the Division should prepare a detailed written methodology to follow in preparing and reviewing future billing rates.

Department Corrective Action Plan
SINGLE AUDITOR STATED: An amount of $552,650, which the Division reimbursed the general fund for fringe benefits, was not deducted before adding the federally approved fringe benefit rate of 29%. This resulted in an $552,650 over recovery on all rates.

ITD AGREES WITH THE SINGLE AUDITOR: Object D09 should be netted from the calculated amount for fringe benefits. An adjustment will be made in the fiscal year 2000 federal reconciliation for this amount.

SINGLE AUDITOR STATED: The amount included for lease purchases was understated by $1,209,642 resulting in an under recovery on all rates.

The salary of one individual was added in twice resulting in an $70,269 over charge on the network.

The amounts deducted for capital equipment and added for depreciation were from the 1997 final rates. This resulted in a net $842,914 under recovery which applied to all rates.

ITD AGREES WITH THE SINGLE AUDITOR: Inadvertently, two schedules, a variance reconciliation of the Cost Allocation Plan costs to MMARS and a depreciation schedule was not completed. This was an oversight and has not happened in 16 years of preparing the year end reconciliation. Consequently, the above costs were incorrectly accounted for or omitted from the final rate calculation. These costs will be added or subtracted from the fiscal year 2000 reconciliation.

SINGLE AUDITOR STATED: The amounts deducted for equipment use allowance were from the 1997 final rates. This resulted in an over recovery of $41,491 applicable to all rates.

The amounts deducted for equipment use allowance were from the 1997 final rates. This resulted in an over recovery of $41,491 applicable to all rates.

ITD DISAGREES WITH THE SINGLE AUDITOR: The amount is correct. There were no additions to the equipment use allowance schedule in fiscal year 1998. No adjustment will be made.

SINGLE AUDITOR STATED: Commonwealth received approval of the 1998 SWCAP after the 1998 rates were prepared. As a result, the amounts used in the rates for the executive office allocation was understated by $1,556,578 and the state-wide cost allocation plan (SWCAP) amount was overstated by $10,765. An additional amount of $1,545,813 can be added as an under recovery for 1998.

ITD AGREES WITH THE SINGLE AUDITOR: The new SWCAP rate was not available at preparation time. This amount will be added to the fiscal year 2000 reconciliation.

SINGLE AUDITOR STATED: The rate used to compute space use was $16.67/square foot, which was the rate in the previously approved SWCAP. The rate subsequently approved in the SWCAP was $15.02. This resulted in a $28,958 over recovery on all rates.

ITD AGREES WITH THE SINGLE AUDITOR: The new SWCAP rate was not available at preparation time. This amount will be subtracted from the fiscal year 2000 reconciliation.

SINGLE AUDITOR STATED: Total Division costs before adjustment for the items noted above was $30,294,413. Revenue as recorded in MMARS was $11,022,416 for a net under recovery of $19,271,997. The net over/under recovery by service could not readily be determined.

ITD DISAGREES WITH THE SINGLE AUDITOR: The auditor's assertions are incorrect.

There is some confusion. ITD manages two separate and distinct chargeback systems. One system is a federally approved cost allocation plan. The second is authorized by the state legislature. The systems run in parallel and appear to be one in the same since they are combined onto one monthly invoice. From a business point of view it makes sense to issue one monthly chargeback invoice as oppose to two invoices. Issuing one chargeback invoice eliminates confusion and cost.

The ITD ADP Cost Allocation Plan (Federal chargeback) is a federally approved plan operating under the rules of OMB Circular A-87, ASMB C-10 and 45 CFR 95 Subpart F. Under these rules, the Federal chargeback system billed but did not collect $30 million to all ITD client agencies. A year-end reconciliation for each client agency by service type was provided to the auditor.

The Statewide chargeback system is authorized by the State Legislature. The Statewide chargeback system billed out and collected $11 million via the MMARS Intra-governmental voucher process. This was consistent with the authorizing State legislation.

The Federal chargeback system has been operating for 6 years longer than the Statewide system. The

Federal chargeback system has been in existence since Fiscal Year 1982 and the Statewide since Fiscal Year 1988.

There are differences between the two systems. The Statewide chargeback system is authorized to bill out the cost of the Data Center, the Mailroom operation and the Communications Services Bureau. Other parts of ITD are not charged out. Imputed costs for floor space, amounts attributable to ITD from the SWCAP and fringe benefit costs not included in object code D09 are not billed out. In some years the legislature permitted ITD to charge out the Information Warehouse and in other fiscal years ITD was not permitted to bill for the Warehouse. The rate methodologies are for the most part the same, however, in some cases they differ. Moreover, some agencies have exempted themselves, via state legislation, from being charged. Unlike the Statewide chargeback system, the federal chargeback cost allocation plan bills all client agencies for the entire cost of ITD including the imputed costs that are not part of the ITD budget.

Another difference between the two systems: the Statewide system's charges are substantially less than the Federal chargeback system. The Statewide system gives a credit to the client agency based on the agency's prior year computer resource usage. The "ITD Credit" represents the portion of the Data Center, the Mailroom operation and the Communications Service Bureau that is directly funded by the State Legislature. During fiscal year 98 this amount was approximately 45% of the operating cost of the billed out cost centers. The "ITD Credit" is not allocated by service type but is allocated in one lump sum to each client agency and applied in 12 equal installments throughout the fiscal year. Moreover, State Legislation does not require a breakdown by service type.

ITD believes the Statewide system is out of the scope of the Single Audit of the ITD ADP Cost Allocation Plan. ITD asserts that the Intra-governmental revenues billed via the MMARS/ IV process are not to be construed as revenues billed and collected for Federal chargeback purposes. Moreover, ITD asserts that having two chargeback systems, separate and distinct are consistent with Federal regulations and with State legislation.

SINGLE AUDITOR STATED: The Division stated that the miscalculations were an oversight and that it was not aware that the 1998 SWCAP was approved after the rates were prepared. The Division does not have a detail step-by-step methodology, which would serve as a checklist to ensure all items are included or adjusted.

ITD DISAGREES WITH THE SINGLE AUDITOR: ITD does have a step-by-step methodology for completing the federal reconciliation. Such a methodology is not within the scope of the audit, it is not required by Circular A-87 and the Auditor did not see it.

More importantly, this was the first time in 16 fiscal years of preparing this reconciliation that two schedules were left out. It is regrettable and efforts will be made to see that oversights will not happen again.

Responsible Individual: David Lewis

Findings not Repeated from Prior Years

1. The Information Technology Division included duplicate unemployment insurance of $25,121 in computing its final 1995 rates. The credit was included in computing the 1998 final rates. *(Fiscal Year 1998 Single Audit Finding 66)*

Next Section
