

February 8, 1995

Mr. Vernon M. Arrell, Commissioner
Texas Rehabilitation Commission
4900 North Lamar Blvd.
Austin, Texas 78751-2316

Dear Mr. Arrell:

The Commission has established a system to ensure compliance with federal regulations for its two largest federal programs, *Rehabilitation Services - Basic Support* and *Disability Determination Services*. These programs represent 96 percent of the Commission's \$193 million of total federal assistance. However, the Commission is not complying with federal cash management funding technique requirements and not adequately supporting their Indirect Cost Rate proposals.

The attached findings and Commission responses will appear in the *1994 Financial and Compliance Audit Results* report. This report contains the audit results of all agencies and universities we visited during the statewide financial and compliance audit.

When this report is published in May 1995, copies will be distributed to the board chairperson and chief executive officer for each agency included. Additional copies can be obtained from Production Services at 479-4700.

A copy of this letter has been sent to each board member. If you have any questions, please call me at 479-4844. I appreciate the cooperation and support provided by you and your staff.

Sincerely,

Donna K. Todd
Project Manager

DKT:ggh

cc: David J. MacCabe, CIA, Associate Commissioner

Key Points of Report

Texas Rehabilitation Commission 1994 Statewide Financial and Compliance Audit

February 1995

Overall Conclusion

The Commission has established a system to ensure compliance with federal regulations for its two largest federal programs, *Rehabilitation Services - Basic Support and Disability Determination Services*. These programs represent 96 percent of the Commission's \$193 million of total federal assistance. However, the Commission is not complying with two federal requirements.

Key Findings

- The Commission is not complying with federal cash management funding technique requirements for the Rehabilitation Services program. The State incurs an interest liability for each day excess funds are held by the Commission.
- The U.S. Department of Health and Human Services' Office of Inspector General reported that the policies and procedures related to the preparation of indirect cost rate proposals are not sufficient to ensure that the proposals are adequately supported. This could result in potential under- or overrecoveries of prior years' indirect costs.

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Federal Compliance Issues

Federal Compliance Issue 1:

Comply With Federal Cash Management Funding Technique Requirements

The Commission is not complying with the federal cash management funding technique requirements for the Rehabilitation Services program (CFDA 84.126).

The Commission requests federal funds ten days before payday to cover payroll expenses. This resulted in excess federal funds on hand for 9 of twenty-one state working days tested. The State incurs an interest liability for each day excess funds are held by the Commission.

Title 31 Code of Federal Regulations (CFR), part 205.7(c)(4) states that federal funds shall not be requested more than three business days prior to disbursement. However, state law requires that sufficient funds be in the State Treasury the tenth day before pay day or the payroll will not be processed. To facilitate compliance with federal regulations, general revenue funds may be temporarily used to cover federal payroll costs [Texas Government Code, section 403.092 (c)]. The Comptroller of Public Accounts must be notified to initiate this transaction.

Recommendation: The Commission should comply with federal cash management requirements. Federal funds should be requested for immediate cash needs no more than three business days prior to disbursement. The Commission should make arrangements with the Comptroller to temporarily transfer general revenue funds to cover federal payroll costs. General revenue funds should be reimbursed as soon as federal funds are received and no later than pay day.

Management's Response: *We agree with the SAO recommendation to comply with federal cash management requirements. Since funding for payroll can be from general revenue on a temporary basis, we will work with the Comptroller as necessary.*

Federal Compliance Issue 2:

Ensure That Indirect Cost Rate Proposals Are Adequately Supported

In a recent review of the 1995 Indirect Cost Rate Proposal draft, the U.S. Department of Health and Human Services' Office of Inspector General reported that the policies and procedures related to the preparation of indirect cost rate proposals are not sufficient to ensure that the proposals are adequately supported. The indirect costs of various pools were incorrectly allocated, and vouchered costs may be overstated on the 1995 Proposal draft. The same methodology that was used to prepare this proposal was used to

prepare previous years' proposals, resulting in potential under- or overrecoveries of prior years' indirect costs.

Office of Management and Budget (OMB) Circular A-87 defines indirect costs as those incurred for a common or joint purpose benefitting more than one objective and which are not readily assignable to the cost objective. Direct costs are those costs that can be identified specifically with a particular cost objective.

It is essential that each item of cost be treated consistently either as direct or indirect. Indirect cost pools should be distributed to benefitting cost objectives on an equitable basis with the benefits derived. In addition, OMB A-87 states that all costs in the plan will be supported by formal accounting records.

Recommendation: The Commission should continue to work with the U.S. Department of Health and Human Services' Office of Inspector General to resolve the issues identified with the 1995 Indirect Cost Proposal draft. The Commission should also revise its policies and procedures to ensure that indirect cost rate proposals are adequately supported, the costs are correctly allocated, the allocation bases are appropriate and equitable, and the cost pools are properly classified and treated consistently. Any under- or overrecoveries of prior years' indirect costs should be reflected in future indirect cost proposals.

Management's Response: *While we do not agree with all of the issues raised by the DHHS IG, we do agree with the recommendation of the State Auditor's Office. We will continue to work with the DHHS IG to resolve the issues and we will take all corrective actions required.*

Audit Scope

The primary focus of our audit was the Commission's administrative controls over its major federal programs. The Rehabilitation Services - Basic Support program received \$114 million and the Disability Determination Services program received \$71 million. These programs represent 96 percent of the Commission's \$193 million of total federal assistance. We gained an understanding of the internal control structure, including the general control environment and federal programs. We tested the internal control structure related to the major federal programs. Specific procedures were used to test compliance with the major federal programs.