



MICHIGAN

OFFICE OF THE AUDITOR GENERAL

AUDIT REPORT

PERFORMANCE AUDIT
OF THE

STATEWIDE COST ALLOCATION PLAN AND
INTERAGENCY BILLING PROCESSES

DEPARTMENT OF TECHNOLOGY, MANAGEMENT, AND BUDGET

October 2014



Doug A. Ringler, C.P.A., C.I.A.
AUDITOR GENERAL

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– Article IV, Section 53 of the Michigan Constitution

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*Performance Audit
Statewide Cost Allocation Plan and
Interagency Billing Processes
Department of Technology, Management,
and Budget*

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The State of Michigan's Statewide Cost Allocation Plan (SWCAP) is the mechanism by which the State identifies, summarizes, and allocates unbilled indirect costs in a logical and systematic manner. The SWCAP also includes financial and billing rate information for billed central service costs directly charged to agencies or funds. The SWCAP is established in accordance with U.S. Office of Management and Budget Circular A-87 to obtain reimbursement from the federal government for Statewide indirect costs.

Audit Objective			Audit Conclusion
Objective 1: To assess the effectiveness of the Department of Technology, Management, and Budget's (DTMB's) efforts to establish and implement the SWCAP.			Effective
Findings Related to This Audit Objective	Material Condition	Reportable Condition	Agency Preliminary Response
Our audit report does not include any findings related to this audit objective.	Not applicable	Not applicable	Not applicable

Audit Objective			Audit Conclusion
Objective 2: To assess the effectiveness of DTMB's processes for recovery of selected central service costs.			Effective
Findings Related to This Audit Objective	Material Condition	Reportable Condition	Agency Preliminary Response
Our audit report does not include any findings related to this audit objective.	Not applicable	Not applicable	Not applicable

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Auditor General

October 21, 2014

Mr. David B. Behen, Director
Department of Technology, Management, and Budget
Lewis Cass Building
Lansing, Michigan

Dear Mr. Behen:

This is our report on the performance audit of the Statewide Cost Allocation Plan and Interagency Billing Processes, Department of Technology, Management, and Budget.

This report contains our report summary; a description of the Statewide Cost Allocation Plan and interagency billing processes; our audit objectives, scope, and methodology; comments; and a glossary of abbreviations and terms.

We appreciate the courtesy and cooperation extended to us during this audit.

Sincerely,

Doug Ringler
Auditor General

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Description of the Statewide Cost Allocation Plan and Interagency Billing Processes

The State of Michigan's Statewide Cost Allocation Plan (SWCAP) is the mechanism by which the State identifies, summarizes, and allocates unbilled indirect costs* in a logical and systematic manner. The SWCAP also includes financial and billing rate information for billed central service costs* directly charged to agencies or funds through internal service funds* and for building occupancy costs through the General Fund. The State's SWCAP is established in accordance with U.S. Office of Management and Budget (OMB) Circular A-87, *Cost Principles for State, Local, and Indian Tribal Governments* (Title 2, Part 225 of the *Code of Federal Regulations*) to obtain reimbursement from the federal government for Statewide indirect costs.

Statewide unbilled indirect costs include the cost of central support services, such as accounting, purchasing, budgeting, payroll, and information systems, provided to operating departments. The Department of Civil Rights; Civil Service Commission; Department of Technology, Management, and Budget (DTMB); Department of Treasury; and Office of the Auditor General provide central support services.

Billed central service costs include goods or services provided primarily to other State agencies or funds rather than to the general public. Some of these goods and services include motor pool services; printing, reproduction, and mailing services; telecommunication and information technology services; health-related fringe benefits; and building occupancy charges.

DTMB's Office of Financial Management is responsible for the State's SWCAP. Since 1987, DTMB has contracted with a private consultant to prepare the SWCAP. DTMB reviews and approves the SWCAP before it is submitted to the U.S. Department of Health and Human Services (HHS).

The State submits to HHS a proposed SWCAP based on current estimated costs and a final SWCAP based on actual costs from a prior period. HHS is the cognizant agency that annually approves the SWCAP and negotiates the Cost Allocation Agreement with DTMB, establishing Statewide indirect costs for the State's operating departments. The

* See glossary at end of report for definition.

Statewide indirect costs are established on a fixed with carry-forward basis*. The most recent Cost Allocation Agreement approved indirect costs for fiscal year 2013-14 and included estimated costs for the fiscal year 2013-14 SWCAP and carry-forward costs from the fiscal year 2011-12 final SWCAP.

DTMB provides the approved Statewide indirect costs to the State's operating departments for allocation to their federal assistance programs. Approved Statewide indirect costs provided to operating departments and other funds for fiscal year 2013-14 were \$97.4 million.

Operating departments are required by Section 18.1460 of the *Michigan Compiled Laws* (Act 431, P.A. 1984) to establish departmental indirect cost rates and to charge indirect costs to awards, contracts, and grants. The departmental indirect costs may include Statewide indirect costs as determined by each operating department's method of billing indirect costs for different federal assistance programs.

State agencies are billed for goods and services based on rates established to cover actual costs. Billed central service costs charged directly to other State agencies or funds were as follows:

	Fiscal Year	
	2012-13	2011-12
State Sponsored Group Insurance Fund	\$ 727,946,000	\$ 730,153,000
Information Technology Fund	\$ 551,802,000	\$ 518,944,000
Office Services Revolving Fund	\$ 102,680,000	\$ 94,379,000
Motor Transport Fund	\$ 65,284,000	\$ 61,557,000
Risk Management Fund	\$ 3,564,000	\$ 4,361,000
Building occupancy	\$ 88,081,766	\$ 86,775,233

* See glossary at end of report for definition.

Audit Objectives, Scope, and Methodology

Audit Objectives

Our performance audit* of the Statewide Cost Allocation Plan (SWCAP) and Interagency Billing Processes, Department of Technology, Management, and Budget (DTMB), had the following objectives:

1. To assess the effectiveness* of DTMB's efforts to establish and implement the SWCAP.
2. To assess the effectiveness of DTMB's processes for recovery of selected central service costs.

Audit Scope

Our audit scope was to examine the Statewide Cost Allocation Plans for fiscal years 2012-13 and 2011-12 and to review the billing processes for selected central service costs. We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our conclusions based on our audit objectives. Our audit procedures, which included a preliminary survey, audit fieldwork, report preparation, and quality assurance, generally covered the period October 1, 2011 through June 30, 2014.

Audit Methodology

We conducted a preliminary survey to gain an understanding of the SWCAP and interagency billing processes and internal control* in order to establish our audit objectives and methodology. During our preliminary survey, we:

- Interviewed DTMB management and staff to obtain an overall understanding of the SWCAP and internal service funds, including DTMB's interagency billing processes, controls, and involvement in the process for preparing the SWCAP reports.
- Reviewed applicable federal regulations and State laws.

* See glossary at end of report for definition.

- Analyzed the internal service fund expenditure and revenue records.
- Met with the consultant who prepares the SWCAP regarding the processes of obtaining data and preparing the SWCAP.

To accomplish our first objective, we:

- Identified key federal and State regulations.
- Reviewed the balance sheets required to be submitted by U.S. Office of Management and Budget (OMB) Circular A-87, *Cost Principles for State, Local, and Indian Tribal Governments* (Title 2, Part 225 of the *Code of Federal Regulations*) to ensure that working capital reserves for the internal service funds did not exceed more than 60 days of cash expenditures.
- Traced a random selection of central service departments' reports within the SWCAP to the financial reports provided by DTMB to the contractor and to accounting records.
- Reviewed the SWCAP section I and II reports to ensure that they met the federal submission requirements.
- Reviewed the federal approval and comments on the prepared SWCAP reports.

To accomplish our second objective, we:

- Reviewed the services provided and the processes used by DTMB for billing State agencies for the costs of central services provided by the internal service funds and the General Fund.
- Documented controls over billings for services provided through the Information Technology Fund, Office Services Revolving Fund, Motor Transport Fund, and building occupancy charges.
- Reviewed a random selection of billings to determine if the billings were based on correct rates and if agencies were properly billed based on the services provided.

COMMENTS

EFFECTIVENESS OF EFFORTS TO ESTABLISH AND IMPLEMENT THE SWCAP

COMMENT

Audit Objective: To assess the effectiveness of the Department of Technology, Management, and Budget's (DTMB's) efforts to establish and implement the Statewide Cost Allocation Plan (SWCAP).

Audit Conclusion: We concluded that DTMB's efforts were effective in establishing and implementing the SWCAP.

Factors leading to this conclusion included:

- Our review of supporting documentation for the amounts used in the SWCAP for selected central service departments did not disclose any significant errors.
- Our review did not identify any instances in which the federal submission requirements were not met.
- DTMB's internal review processes help ensure that the SWCAP is accurate and appropriate.
- Our audit report does not include any findings related to this audit objective.

EFFECTIVENESS OF PROCESSES FOR RECOVERY OF SELECTED CENTRAL SERVICE COSTS

COMMENT

Audit Objective: To assess the effectiveness of DTMB's processes for recovery of selected central service costs.

Audit Conclusion: We concluded that DTMB's processes were effective in recovering selected central service costs.

Factors leading to this conclusion included:

- Our review of supporting documentation for interagency billings did not disclose any significant errors.
- DTMB's internal control and processes help ensure that the interagency billings are appropriate.
- Our audit report does not include any findings related to this audit objective.

GLOSSARY

Glossary of Abbreviations and Terms

central service costs	Central services billed to benefiting agencies on an individual fee-for-service basis.
DTMB	Department of Technology, Management, and Budget.
effectiveness	Success in achieving mission and goals.
fixed with carry-forward basis	A basis for establishing Statewide indirect costs whereby the costs are estimated in the Cost Allocation Agreement and are adjusted for actual costs in a later year.
HHS	U.S. Department of Health and Human Services.
indirect costs	Costs incurred for a common or joint purpose that benefit more than one program or function.
internal control	The plan, policies, methods, and procedures adopted by management to meet its mission, goals, and objectives. Internal control includes the processes for planning, organizing, directing, and controlling program operations. It also includes the systems for measuring, reporting, and monitoring program performance. Internal control serves as a defense in safeguarding assets and in preventing and detecting errors; fraud; violations of laws, regulations, and provisions of contracts and grant agreements; or abuse.
internal service fund	A fund established to account for financial transactions for services provided by a State agency to other State agencies.
material condition	A matter that, in the auditor's judgment, is more severe than a reportable condition and could impair the ability of

management to operate a program in an effective and efficient manner and/or could adversely affect the judgment of an interested person concerning the effectiveness and efficiency of the program.

performance audit

An audit that provides findings or conclusions based on an evaluation of sufficient, appropriate evidence against criteria. Performance audits provide objective analysis to assist management and those charged with governance and oversight in using the information to improve program performance and operations, reduce costs, facilitate decision making by parties with responsibility to oversee or initiate corrective action, and contribute to public accountability.

reportable condition

A matter that, in the auditor's judgment, is less severe than a material condition and falls within any of the following categories: an opportunity for improvement within the context of the audit objectives; a deficiency in internal control that is significant within the context of the audit objectives; all instances of fraud; illegal acts unless they are inconsequential within the context of the audit objectives; significant violations of provisions of contracts or grant agreements; and significant abuse that has occurred or is likely to have occurred.

SWCAP

Statewide Cost Allocation Plan.

