

FINANCIAL RELATED AUDIT  
OF THE  
STATEWIDE INDIRECT COST ALLOCATION PLAN

DEPARTMENT OF MANAGEMENT AND BUDGET

July 1, 1994 through September 30, 1996

# EXECUTIVE DIGEST

## STATEWIDE INDIRECT COST ALLOCATION PLAN

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### INTRODUCTION

This report contains the results of our financial related audit of the Statewide Indirect Cost Allocation Plan (SWICAP), Department of Management and Budget, for the period July 1, 1994 through September 30, 1996.

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### AUDIT PURPOSE

This financial related audit was conducted as part of the constitutional responsibility of the Office of the Auditor General. Financial related audits are conducted at various intervals to permit the Auditor General to express an opinion on the State's financial statements. Also, this audit complements our departmentwide financial audits, including the provisions of the Single Audit Act of 1984, which are conducted pursuant to Act 251, P.A. 1986.

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### BACKGROUND

A SWICAP is the mechanism by which a state identifies, summarizes, and allocates indirect costs\* in a logical and systematic manner. A SWICAP is necessary for the State to obtain reimbursement from the federal government for the costs of central support services provided to operating departments by the Department of Civil Rights, Department of Civil Service, Department of Management and Budget (DMB), Department of Treasury, and Office of the Auditor General.

The State prepares both a proposed SWICAP based on estimated costs and a final SWICAP based on actual costs. The U.S. Department of Health and Human Services (HHS) is the cognizant agency that annually approves the State's SWICAP on a fixed cost basis with a carry-forward

\* See glossary on page 14 for definition.

\*agreement. This agreement allows the State to base its proposed SWICAP on estimated costs. The difference between the estimated costs in the proposed SWICAP and the actual costs in the final SWICAP for each fiscal year is included as an adjustment in the subsequent year=s proposed SWICAP. Because of the nature of this process and the timing of it, the SWICAP for fiscal year 1993-94 was the most current SWICAP with final approval at the time of our review.

The DMB Office of Financial Management is responsible for the State's SWICAP. Since 1986, DMB has contracted with a private consultant to prepare the SWICAP.

For fiscal year 1993-94, the State received \$6 billion in federal funds. Of this amount, \$14.2 million was recovered in indirect costs.

#### AUDIT OBJECTIVES AND CONCLUSIONS

**Audit Objective:** To assess the allowability of costs (per Office of Management and Budget Circular A-87) included in the SWICAP.

**Conclusion:** Our assessment of costs included in the SWICAP disclosed that they were allowable.

**Audit Objective:** To assess the reasonableness of the SWICAP methodology used to allocate central support service costs to user departments.

**Conclusion:** Our assessment of the allocation methodology disclosed that it was reasonable.

**Audit Objective:** To assess whether the SWICAP included all documentation required by HHS.

**Conclusion:** Our assessment of SWICAP documentation disclosed that all required documentation was included.

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**Audit Objective:** To assess the timeliness of DMB's distribution of SWICAP costs to departments and to assess whether DMB ensured that departmental indirect cost proposals included the correct SWICAP costs.

**Conclusion:** Our assessment disclosed that DMB distributed SWICAP costs to departments in a timely manner and ensured that departmental indirect cost proposals included the correct SWICAP costs.

**Audit Objective:** To assess whether the internal service funds\* which were included in the SWICAP complied with the federal allowance for retained earnings.

**Conclusion:** Our assessment disclosed that the internal service funds' retained earnings at September 30, 1995 were in compliance with the federal allowance for retained earnings (up to 60 days of a fund's cash operating expenditures) except for microfilm operations. As of September 30, 1995, the amount of the questioned costs related to microfilm operations was approximately \$131,000 (see schedule of questioned costs).

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**AUDIT SCOPE**

Our audit scope was to examine the State's Statewide Indirect Cost Allocation Plans which were completed in our audit period. Our audit scope was mainly to examine the final SWICAP for fiscal year 1993-94. We also examined the proposed SWICAP's for fiscal years 1994-95 and 1995-96. Our audit was conducted in accordance with *Government Auditing Standards* issued by the Comptroller General of the United States and, accordingly, included such tests of the records and such other auditing procedures as we considered necessary in the circumstances.

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**PRIOR AUDIT  
FOLLOW-UP**

DMB had complied with the one prior audit recommendation.

\* See glossary on page 14 for definition.

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Mr. Mark A. Murray, Director  
Department of Management and Budget  
Lewis Cass Building  
Lansing, Michigan

Dear Mr. Murray:

This is our report on the financial related audit of the Statewide Indirect Cost Allocation Plan (SWICAP), Department of Management and Budget, for the period July 1, 1994 through September 30, 1996.

This report contains our executive digest; description of the SWICAP; audit objectives, audit scope, and prior audit follow-up; comments; schedule of questioned costs, presented as supplemental information; and a glossary of acronyms and terms.

Our comments are organized by audit objective.

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

AUDITOR GENERAL

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## **Description of the Statewide Indirect Cost Allocation Plan**

A Statewide Indirect Cost Allocation Plan (SWICAP) is the mechanism by which a state identifies, summarizes, and allocates indirect costs in a logical and systematic manner. A SWICAP is necessary for the State to obtain reimbursement from the federal government for Statewide indirect costs.

Statewide indirect costs include the cost of central support services provided to operating departments. The Department of Civil Rights, Department of Civil Service, Department of Management and Budget (DMB), Department of Treasury, and Office of the Auditor General provide central support services.

The U.S. Department of Health and Human Services (HHS) is the cognizant agency that approves each state's SWICAP.

The State prepares both a proposed SWICAP for each fiscal year based on estimated costs and a final SWICAP based on actual costs. HHS annually approves the State's SWICAP on a fixed cost basis with a carry-forward agreement. This agreement allows the State to base its proposed SWICAP on estimated costs. The difference between the estimated costs in the proposed SWICAP and the actual costs in the final SWICAP for each fiscal year is included as an adjustment in the subsequent year's proposed SWICAP. Because of the nature of this process and the timing of it, the SWICAP for fiscal year 1993-94 was the most current SWICAP with final approval at the time of our review.

The State's annual SWICAP agreement with HHS also contains compliance requirements for internal service funds which charge federal programs for services.

The DMB Office of Financial Management is responsible for the State's SWICAP. Since 1986, DMB has contracted with a private consultant to prepare the SWICAP. DMB reviews and approves the SWICAP before it is submitted to HHS.

For fiscal year 1993-94, the State received \$6 billion in federal funds. Of this amount, \$14.2 million was recovered in indirect costs.

## **Audit Objectives, Audit Scope, and Prior Audit Follow-Up**

### Audit Objectives

Our financial related audit of the Statewide Indirect Cost Allocation Plan (SWICAP), Department of Management and Budget (DMB), had the following objectives:

1. To assess the allowability of costs (per Office of Management and Budget Circular A-87) included in the SWICAP.
2. To assess the reasonableness of the SWICAP methodology used to allocate central support service costs to user departments.
3. To assess whether the SWICAP included all documentation required by the U.S. Department of Health and Human Services.
4. To assess the timeliness of DMB's distribution of SWICAP costs to departments and to assess whether DMB ensured that departmental indirect cost proposals included the correct SWICAP costs.
5. To assess whether the internal service funds which were included in the SWICAP complied with the federal allowance for retained earnings.

Our audit relative to the objectives for the assessment of allowability of costs, reasonableness of methodology, and compliance with OMB Circular A-87 for the SWICAP complements our departmentwide financial audits, including the provisions of the Single Audit Act of 1984, which are conducted pursuant to Act 251, P.A. 1986.

### Audit Scope

Our audit scope was to examine the State's Statewide Indirect Cost Allocation Plans which were completed in our audit period. Our audit scope was mainly to examine the final SWICAP for fiscal year 1993-94. We also examined the proposed SWICAP's for fiscal years 1994-95 and 1995-96. Our audit was conducted in accordance with *Government Auditing Standards* issued by the Comptroller General of the United States and, accordingly, included such tests of the records and such other auditing procedures as we considered necessary in the circumstances.

### Prior Audit Follow-Up

DMB had complied with the one prior audit recommendation.

## COMMENTS

### ALLOWABILITY OF COSTS

#### COMMENT

**Audit Objective:** To assess the allowability of costs (per Office of Management and Budget Circular A-87) included in the Statewide Indirect Cost Allocation Plan (SWICAP).

**Conclusion:** Our assessment of costs included in the SWICAP disclosed that they were allowable.

### COST ALLOCATION METHODOLOGY

#### COMMENT

**Audit Objective:** To assess the reasonableness of the SWICAP methodology used to allocate central support service costs to user departments.

**Conclusion:** Our assessment of the allocation methodology disclosed that it was reasonable.

### DOCUMENTATION

#### COMMENT

**Audit Objective:** To assess whether the SWICAP included all documentation required by the U.S. Department of Health and Human Services (HHS).

**Conclusion:** Our assessment of SWICAP documentation disclosed that all required documentation was included.

## **DISTRIBUTION OF SWICAP COSTS TO DEPARTMENTS**

### COMMENT

**Audit Objective:** To assess the timeliness of the Department of Management and Budget's (DMB's) distribution of SWICAP costs to departments and to assess whether DMB ensured that departmental indirect cost proposals included the correct SWICAP costs.

**Conclusion:** Our assessment disclosed that DMB distributed SWICAP costs to departments in a timely manner and ensured that departmental indirect cost proposals included the correct SWICAP costs.

## **INTERNAL SERVICE FUNDS**

### COMMENT

**Audit Objective:** To assess whether the internal service funds which were included in the SWICAP complied with the federal allowance for retained earnings.

**Conclusion:** Our assessment disclosed that the internal service funds' retained earnings at September 30, 1995 were in compliance with the federal allowance for retained earnings (up to 60 days of a fund's cash operating expenditures) except for microfilm operations.

Microfilm operations are accounted for as a subfund of the Office Services Revolving Fund, an internal service fund administered by DMB. HHS has informed DMB that each subfund of the Office Services Revolving Fund must comply with the federal internal service fund retained earnings requirements. As of September 30, 1995, the amount of the questioned costs was approximately \$131,000 (see schedule of questioned costs).

When retained earnings for a fund exceed the 60-day allowance, HHS either requires the State to make a payment for the federal share of the excess or allows the State to reduce the excess by adjusting the billings for the fund. DMB had prepared a federal report which indicated that the excess retained earnings for microfilm operations were approximately \$131,000. As of December 1996, DMB had not submitted this report to HHS for determination of the disposition to be made.

# SUPPLEMENTAL INFORMATION

STATEWIDE INDIRECT COST ALLOCATION PLAN

Department of Management and Budget

Schedule of Questioned Costs

<u>Program</u>	<u>Finding</u>	<u>Questioned Costs</u>
Microfilm Operations	Retained earnings as of September 30, 1995 exceeded federal guidelines that allow up to 60 days of an internal service fund's cash operating expenditures.	\$ <u>131,000</u>
	Total Questioned Costs	\$ <u><u>131,000</u></u>

## **Glossary of Acronyms and Terms**

<b>DMB</b>	Department of Management and Budget.
<b>HHS</b>	U.S. Department of Health and Human Services.
<b>indirect costs</b>	Costs incurred for a common or joint purpose that benefit more than one program or function.
<b>Internal service fund</b>	A fund established to account for financial transactions for services provided by a State agency to other State agencies.
<b>SWICAP</b>	Statewide Indirect Cost Allocation Plan.