INVESTIGATIVE AUDIT

Oklahoma State Department of Health

For the period July 1, 2010 through February 28, 2018

Oklahoma State
Auditor & Inspector
Gary A. Jones, CPA, CFE

Investigative Audit Report of the Oklahoma State Department of Health

For the Period July 1, 2010 through February 28, 2018

Oklahoma State Auditor & Inspector

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May 15, 2018

TO THE HONORABLE MIKE HUNTER, OKLAHOMA ATTORNEY GENERAL

Pursuant to your request and in accordance with the requirements of 74 O.S. § 18(f), we performed an audit with respect to the Oklahoma State Department of Health for the period July 1, 2010 through February 28, 2018.

The objectives of our audit primarily included, but were not limited to, the concerns surrounding the agency's financial condition. The results of this audit, related to these objectives, are presented in the accompanying report.

Because the procedures performed do not constitute an audit conducted in accordance with generally accepted auditing standards, we do not express an opinion on the account balances or financial statements of the Oklahoma State Department of Health for the period July 1, 2010 through February 28, 2018.

We also wish to take this opportunity to express our appreciation for the assistance and cooperation extended to our office during the course of our engagement.

Sincerely,

Gary A Jones

GARY JONES, CPA, CFE
OKLAHOMA STATE AUDITOR & INSPECTOR

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Oklahoma State Department of Health

Investigative Audit Report

Executive Summary

Background

In the late summer and early fall of 2017, officials with the Oklahoma State Department of Health (OSDH or agency) began "sounding the alarm" regarding inappropriate accounting practices, financial mismanagement, and dire financial circumstances at the agency.

The officials' concerns were first brought to the attention of the State Auditor and Inspector's office during an audit of the expenditures at OSDH for the State of Oklahoma's Comprehensive Annual Financial Report (CAFR). As the audit process moved forward[1], the officials' concerns were reiterated and were also included in testimony before the Oklahoma House of Representatives Special Investigative Committee. They specifically mentioned that the agency was experiencing a $30 million shortfall due to current year "borrows" and "payroll not posted" (PNP).

Subsequently, an urgent request for a $30 million emergency supplemental appropriation was made. OSDH's corrective action report provided to the legislature stated that a "critical infusion of funds in the amount of $30 million . . . allowed OSDH to stabilize payroll and turn its attention to issues causing the staggering financial crisis in which OSDH finds itself."

What We Found

- The agency did not need the $30 million emergency special appropriation. Based on our analysis, at no point during the time period of June 2017 through February 2018 was the agency's un-restricted cash insufficient to meet payroll needs. (See page 36)
- The agency may have unnecessarily terminated 198 employees. The lack of need for the $30 million indicates that all or part of the cost saving efforts related to those terminations may not have been required. In addition, cost savings projections were inconsistent and inaccurate and the terminations will not result in the savings claimed in the Reduction In Force (RIF) plan submitted to the Office of Management and Enterprise Services (OMES). (See pages 38 - 40)

[1] A special audit was originally requested by the Commissioner of Health in September 2017. This audit was subsequently revised in November 2017 to a special investigation under the authority of the Attorney General's office in accordance with 74 O.S. § 18(f).

- The State Board of Health (Board) failed to exercise its fiduciary responsibility as required by state statutes and best practices. (See page 6)
- Senior management created a hostile work environment, poor control environment, and poor tone at the top. (See page 10)
- Senior management inflated budgets and promoted an increasing trend of expending funds in excess of revenues received by the agency. (See page 12)
- The agency inappropriately advanced $8.5 million to the Tobacco Settlement Endowment Trust (TSET) and $1.5 million to the Oklahoma University Health Sciences Center (OUHSC). (See page 22)
- All federal funds, and Ryan White restricted rebate funds, are comingled in the 400 fund at OMES. (See page 34)

How Did This Happen?

OSDH management was relying almost entirely on information obtained from an outdated internal accounting system (FISCAL) that duplicates the statewide accounting system, and on inappropriate unorthodox accounting practices (such as internal borrows, payroll not posted, and program funds recovered) that did not reflect reality. The agency has made some efforts in the past to discontinue the use of FISCAL and convert to the State of Oklahoma's statewide accounting system as their primary accounting system. However, after spending $3.6 million on this project, and anticipating additional expenditures, they walked away with no tangible results.

Although the agency claimed that the current financial "crisis" is due in part to decreasing revenues, that claim does not reflect the full picture. While appropriated revenues decreased $7 million between fiscal year (FY) 2011 and FY 2017, non-appropriated revenues increased $20 million during the same time period. In summary, total agency revenues increased by $13 million and total overall expenditures increased by $15 million.

The concerns regarding the agency's financial position were compounded by a negative control environment set by senior management. In addition to the tone at the top issues, there was a large amount of turnover in key financial positions such as the Chief Financial Officer (CFO). At one point, this position went vacant for approximately one year. Not only did this result in the loss of key institutional knowledge, it resulted in lack of appropriate financial oversight. Negative attitudes of staff toward senior management, as communicated to us during interviews, impacted morale and increased risk. The magnitude of this negativity is a red flag regarding the agency's general environment and tone at the top, and validates that this is a real and pervasive issue.

Finally, the Board did not perform its fiduciary duties during this time period as mandated by state law and best practices. Its failure to appropriately communicate with key financial personnel or require sufficient and appropriate financial information to perform their duties clearly contributed to the overall situation.

How Do We Fix It?

The complex problems at OSDH will require an equally multi-faceted solution. We recommend at a minimum that:

- The Board and the Commissioner make every effort to improve the control environment and tone at the top of the agency
- OSDH immediately discontinue inappropriate unorthodox accounting practices and move toward using the statewide accounting system
- OSDH hire a CFO and Controller experienced with federal grant reporting and state accounting practices to fill the currently vacant positions
- OSDH immediately begin preparing and submitting budgets that are realistic and based on known and historical data and ensure that expenditures do not exceed revenues
- OMES establish a separate restricted fund for the Ryan White program rebates
- The legislature consider recalling all or part of the $30 million emergency special appropriation
- The OSDH Board should work towards fulfilling its fiduciary responsibilities for the agency as outlined in state statutes and best practices. When the duties and powers of the Board are transferred to the State Commissioner of Health in January 2019 as outlined in HB 3036, the Commissioner can benefit from following this same recommendation.

Background

For more than one hundred years – first as the Territorial Board of Health then, following statehood, as the Oklahoma Department of Health – the agency has been entrusted by the people of Oklahoma to be the state's prudent stewards of public health.

Today, the Board has nine members appointed by the governor with senate confirmation. The Board appoints the commissioner of health who coordinates activities of the agency with the federal government and other agencies, and directs activities of county health departments.

Each county has a board of health with authority to establish a health department. Through this system of local health services delivery, the OSDH protects and improves the health status of Oklahoma communities through strategies that focus on preventing disease and promoting health. Seventy counties operate health departments. Of those seventy counties, Oklahoma and Tulsa counties are served by autonomous city-county health departments, which enforce and administer Board rules and are administratively different.

According to information compiled by the Oklahoma Department of Libraries[2], OSDH has 1,484 classified employees, 510 unclassified employees, and 83 temporary employees. The agency also has eleven advisory boards. Its mission statement is: "To protect and promote health, to prevent disease and injury, and to cultivate conditions by which Oklahomans can be healthy."

One area of focus that has seen significant expansion in recent history is that of improving health outcomes for Oklahomans. This was a key part of Governor Fallin's campaign platform and initiatives after coming into office in 2011. In response to the governor's initiatives, the Board created the Center for the Advancement of Wellness in 2011, which primarily addresses anti-obesity, anti-tobacco, and other wellness initiatives. During the time period of FY 2011 through FY 2017, the agency spent approximately $120 million on these initiatives.

The agency has diverse sources of revenue that include state appropriations, nearly 50 federal grants, county millage reimbursements, and fee-based revenues (see table on next page).

[2] According to the *Agencies, Boards, and Commissions* Book issued by the Department of Libraries on September 12, 2017

Revenues for FY 2011 through FY 2017 were as follows:

	FY 11	FY 12	FY 13	FY 14	FY 15	FY 16	FY 17
Appropriations	61,533,119	61,800,479	62,964,574	64,689,694	55,547,338	56,109,667	54,884,356
Taxes	20,174,466	21,645,688	20,943,217	18,919,337	18,204,845	18,495,516	18,515,296
Licenses, Permits, Fees	31,762,379	30,621,690	32,041,460	34,219,666	35,527,185	34,730,233	34,158,848
Fines, Forfeits, Penalties	1,578,926	757,468	1,778,258	2,486,615	1,495,995	1,488,145	1,885,337
Income from Money & Prop.	7,312	9,850	2,876	1,156	2,194	5,655	22,245
Grants, Refunds, Reimb.	195,775,241	199,623,003	198,696,992	200,726,290	207,695,201	209,032,533	212,607,529
Sales and Services	16,512,632	16,202,232	15,962,389	15,038,977	12,386,565	21,927,887	16,835,819
Non-Rev. Receipts	7,255,500	6,550,106	6,973,698	6,684,565	4,285,312	5,095,923	9,215,051
Total	**334,599,574**	**337,210,516**	**339,363,464**	**342,766,300**	**335,144,635**	**346,885,559**	**348,124,481**

Source: Combining Trial Balance (revenues presented at the major category level)

Governance

Fiduciary Responsibility

The Board was established by 63 O.S. § 1-103, and consists of nine members selected in a representative fashion from all areas of the state, appointed by the Governor, and confirmed by the Senate for staggered terms of nine years. The Board must include at least four members currently licensed to practice medicine in the State of Oklahoma.

The powers and duties of the Board are enumerated in 63 O.S. § 1-104(B) and include the following:

1. Appoint and fix the compensation of a State Commissioner of Health;
2. Adopt such rules and standards as it deems necessary to carry out any of the provisions of this Code;
3. Accept and disburse grants, allotments, gifts, devises, bequests, funds, appropriations, and other property made or offered to it; and
4. Establish such divisions, sections, bureaus, offices, and positions in the State Department of Health as it deems necessary to carry out the provisions of this Code.

Number three above clearly indicates that the Board has a fiduciary responsibility for the agency and is not limited to an advisory role or merely providing guidance regarding strategic policy. Although the detailed execution of these responsibilities may be delegated by the Board to a State Commissioner of Health, doing so does not relieve the Board of its statutory obligation to ensure financial oversight and proper administration of the agency. Based on testwork performed, the Board abdicated its fiduciary responsibility by failing to request and require sufficient financial information to properly perform its duties.

Best Practices

Based on our review of Board meeting minutes, interviews of Board members, interviews of OSDH staff, and other testwork performed, the Board did not follow best practices[3] in the following areas:

- **Fiduciary responsibility** – Best practices dictate that while it is appropriate to delegate the daily operations of the agency, the Board cannot delegate their statutory responsibility for financial oversight. Although they may have taken more recent steps to at least partially exercise their responsibilities in this area, it appears

[3] Information for best practices obtained from: *The Guide to Not-for-Profit Governance*; Weil, Gosthal, & Manges LLP (2012); *Best Practices for the Executive Directors and Boards of Nonprofit Organizations*; Whatcom Council for Nonprofits; *Best Practice – Audit Committees,* The Government Finance Officers Association (GFOA)

that they did not fulfill their fiduciary responsibilities during the audit period.

- **Communication** – Best practices dictate that the Board should establish open lines of communication with senior financial staff to facilitate the exchange of information. Obtaining comprehensive and accurate financial information is critical to the Board's ability to fulfill their statutory fiduciary responsibilities. This does not appear to have happened during our audit period. Rather than establishing direct communication with those who could provide the needed financial information, the Board relied on often minimal financial information that had been screened, and in some cases altered, by the Senior Deputy Commissioner. We did not discover any evidence of the Board directly requesting or requiring sufficient financial information to fulfill their fiduciary responsibilities.

- **Monitoring** – Best practices dictate that the Board, and the audit committee specifically, monitor and ensure the integrity of the organization's financial reporting processes. We did not discover any substantial evidence of the Board or audit committee doing this during our audit period.

Financial Reporting and Board Involvement

We reviewed Board meeting minutes for the period of January 2010 through August 2017. Our review largely corroborated information we gathered during interviews with current and former agency employees.

Most meeting minutes included a general discussion regarding the agency's budget-to-actual expenditures utilizing what was internally referred to as a "stoplight" report (see example below). One notable missing element is a comparison of expenditures to actual revenues; such information is not presented. There is also no consideration of cash balances and the current financial position of the agency.

SFY 2017 BUDGET AND EXPENDITURE FORECAST: AS OF 05/26/2017

Division	Current Budget	Expenditures	Obligations	Forecasted Expenditures	Not Obligated or Forecasted	Performance Rate
Public Health Infrastructure	$ 21,836,428	$ 13,595,662	$ 4,889,329	$ 2,985,408	$ 366,029	98.32%
Protective Health Services	$ 60,526,021	$ 42,545,956	$ 4,293,073	$ 13,513,195	$ 173,797	99.71%
Office of State Epidemiologist	$ 58,220,933	$ 36,968,611	$ 14,883,338	$ 6,203,379	$ 165,605	99.72%
Health Improvement Services	$ 32,502,699	$ 18,036,168	$ 5,409,556	$ 8,594,975	$ 462,000	98.58%
Community & Family Health Services	$ 222,635,489	$ 152,156,605	$ 12,928,548	$ 57,545,364	$ 4,972	100.00%
Totals:	**$ 395,721,570**	**$ 263,303,002**	**$ 42,403,844**	**$ 88,842,321**	**$ 1,172,403**	99.70%

< 90%	90% - 95%	95% - 102.5%	102.5% - 105%	>105%

Source: OSDH Board Packet

In approximately April 2013, the Board finance committee chair began including a "Finance Brief" with the committee report that included a slightly more detailed discussion of the area of focus chosen for that month. Examples of focus areas included funds used by the agency, and the appropriations process.

Although meeting minutes included discussions and presentations regarding budget cuts and potential cuts in appropriated funds, we noted no indication of consideration of budget-to-actual revenues, cash balances, or overall financial condition of the agency by the Board on a systematic basis.

Most meeting minutes also included a very general report from the Audit, Ethics, and Accountability Committee chair stating that there were "no known significant audit issues to report at this time." Rare exceptions included meetings where the Board approved the annual internal audit plan for the upcoming year.

During interviews with the Board President, Board Vice-President (Chair of Audit, Ethics, and Accountability Committee), and a Board member (chair of finance committee) each one revealed that they had only been involved with agency finances at a very high level. One Board member noted that this seemed appropriate based on the nature of the Board and their status as volunteer Board members. Their primary interest in being on the Board was as "passionate advocates of healthcare," and not to provide financial oversight.

When asked if they felt they had received appropriate financial information, all three expressed that the stop-light report was appropriate for their roles. Two of the three interviewees believed that financial information had been filtered or condensed, particularly by the Senior Deputy Commissioner. They noted that this person was "heavy-handed" with OSDH employees but reasoned at the time that it may have been necessary for an organization of that size. Current and former employees in financial positions recounted meetings where financial staff were reluctant to speak. In those meetings, all questions were answered by the Senior Deputy Commissioner or the Business Planning Director.

All three interviewees agreed that they did not become aware of the severity of the financial issues at OSDH until an October 18, 2017 meeting between the three of them, the Chief Financial Officer, the Chief Operating Officer, the Chief of Internal Audit, and the Legislative Liaison. According to the Board members, they had been notified prior to this meeting that the agency was experiencing a financial shortfall but were reassured by the Commissioner of Health and the Senior Deputy Commissioner that the efforts being undertaken by the agency would be sufficient to address the financial problems faced. However, this timeline appears to be contradicted by information we were provided by the Chief of Internal Audit showing that he had contacted one of the Board members on September 8th and 9th, 2017 suggesting a "sense of urgency" from the financial staff regarding the agency's financial position and specific details regarding his concerns.

During our audit, we became aware of two confidential special investigations performed by the OSDH Office of Accountability Systems (OAS) based on complaints regarding hostile work environments, tone at the top[4], and discrepancies in human resources practices. Based on our discussions with Board members and OAS staff, these matters were appropriately reported to the Board for consideration and action because executive management of the agency was implicated in the complaints. We were unable to find any evidence that the Board responded to the complaints in a substantive manner.

[4] Tone at the Top is discussed further in the Control Environment section.

Control Environment

Negative Control Environment and Inadequate Communication

Management's ethics, integrity, attitude, and operating style are the foundation of all other internal control components that help an entity achieve its objectives and minimize risk. According to government accounting standards[5], an effective internal control system has in place policies and procedures that reduce the risk of errors, fraud, and professional misconduct within the organization. Key factors in this system are the environment established by management, and effective information and communication to achieve the agency's objectives. In addition, standards suggest management needs to assess relevant and reliable communication related to internal and external events.

The agency-wide control environment has a *pervasive* influence that affects all business decisions and activities of the organization. The governing board, chief executive officer, and entire management team must all contribute to creating a positive control environment or "tone at the top." The governing board sets the proper tone for the control environment when it establishes and communicates a code of ethics, requires ethical and honest behavior from all employees, observes the same rules it expects others to follow, and requires appropriate conduct from everyone in the organization. Management's philosophy and methods of employee direction and development also greatly influence this environment.

Tone at the top and throughout the agency is fundamental to an effectively functioning internal control system. Without strong ethical leadership, awareness of risk can be undermined, responses to risk may be inappropriate, control activities may be ill-defined or not followed, information and communication may falter, and feedback from monitoring activities may not be heard or acted upon. Therefore, tone can be either a driver or a barrier to internal control, influencing the control consciousness of all employees.

In addition, the Statewide Accounting Manual for the State of Oklahoma in paragraph 70.10.01 states, "Management's attitude, actions, and values set the tone of an organization, influencing the control consciousness of its people. Internal controls are likely to function well if management believes that those controls are important and communicates that view to employees at all levels. If management views internal controls as unrelated to achieving its objectives, or even worse, as an obstacle, this attitude will also be communicated."

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[5] The United States Government Accountability Office's *Standards for Internal Control in the Federal Government* (2014 Revision)

Throughout our interviews of twenty-one current and previous OSDH employees who had direct interaction with senior management in some capacity, we were made aware of situations regarding the control environment at the central office in Oklahoma City. The following general concerns were expressed about the OSDH senior management:

- An atmosphere of mistrust and poor communication exists;
- Decisions are not effectively communicated to employees;
- Integrity and ethical values are questioned;
- Personnel turnover in finance impacted the division's ability to effectively perform its function;
- Employees are treated unfairly and favoritism exists;
- Employees receive no direction but ample criticism;
- Improprieties are not addressed in a timely and appropriate manner;
- Employees who report improprieties are subject to reprisal;
- A culture of fear exists where long-term employees are afraid to contradict senior management for fear of losing their jobs and impacting their state retirements; and
- The Board is not well informed and has been given misleading financial information.

The magnitude of negative comments communicated to us during interviews is a red flag about the agency's general environment and tone at the top and validates that this is a real and pervasive issue. The negative impact on the agency's control environment has a universal impact on the overall system of internal control, which increases the risk of errors, misappropriation of assets, and decreases quality of services provided. At a time of significant statewide budget issues, a positive work environment and employee satisfaction are integral to retaining staff and maintaining quality of services provided.

Financial Management

Budget, Revenues, and Expenditures

Expenditures Compared to Actual Revenues (cash basis)

We performed a cash-basis analysis (see below) for FY 2011 through FY 2017 comparing total expenditures to total revenues using Combining Trial Balance reports from the statewide accounting system.

Revenues	FY 2011	FY 2012	FY 2013	FY 2014	FY 2015	FY 2016	FY 2017	TOTAL
Total Revenues	$ 273,066,455	$ 275,410,036	$ 276,398,889	$ 278,076,606	$ 279,597,297	$ 290,775,892	$ 293,240,126	$ 1,966,565,301
Total Appropriations	61,533,119	61,800,479	62,964,574	64,689,694	55,547,339	56,109,667	54,884,356	417,529,227
Total Revenues/Appropriations	**$ 334,599,574**	**$ 337,210,515**	**$ 339,363,463**	**$ 342,766,300**	**$ 335,144,636**	**$ 346,885,559**	**$ 348,124,482**	**$ 2,384,094,528**
Expenditures	**FY 2011**	**FY 2012**	**FY 2013**	**FY 2014**	**FY 2015**	**FY 2016**	**FY 2017**	**TOTAL**
Total Personnel Expenditures	$ (133,329,994)	$ (132,783,666)	$ (141,953,145)	$ (147,217,872)	$ (153,432,738)	$ (163,942,365)	$ (152,876,328)	$ (1,025,536,107)
Total Non-Personnel Expenditures	(193,592,310)	(199,199,905)	(198,714,539)	(199,804,506)	(189,388,830)	(199,128,034)	(188,676,360)	(1,368,504,485)
Total Expenditures	**$ (326,922,304)**	**$ (331,983,571)**	**$ (340,667,684)**	**$ (347,022,378)**	**$ (342,821,568)**	**$ (363,070,399)**	**$ (341,552,688)**	**$ (2,394,040,592)**
Ending Revenues Over (Under) Expenditures	**$ 7,677,270**	**$ 5,226,944**	**$ (1,304,221)**	**$ (4,256,078)**	**$ (7,676,932)**	**$ (16,184,840)**	**$ 6,571,794**	**$ (9,946,064)**

Source: Oklahoma Statewide accounting system, Combining Trial Balance Reports

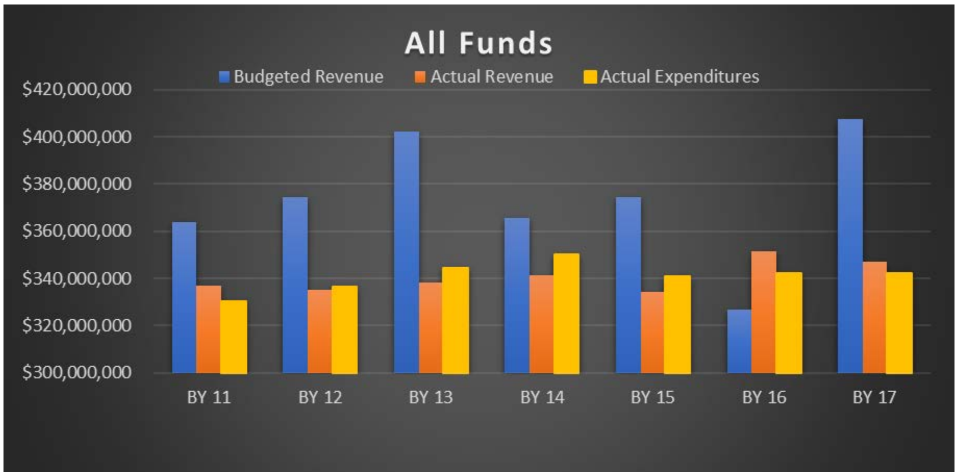
Several important points can be drawn from our analysis (amounts from the table above have been rounded in the following paragraphs):

- Although OSDH has claimed that the current financial "crisis" is due in part to decreasing revenues, that claim does not reflect the full picture of the agency's revenue streams. As reflected in the table above, appropriated revenues have decreased from $62 million in FY 2011 to $55 million in FY 2017. However, during the same time period, non-appropriated revenues increased from $273 million in FY 2011 to $293 million in FY 2017. Overall, total agency revenues increased from $335 million in FY 2011 to $348 million in FY 2017, an increase of $13 million, or 4%.

- Overall expenditures for the agency increased from $327 million in FY 2011 to $342 million in FY2017, an increase of $15 million, or 5%. Personnel (payroll) expenditures increased $20 million with the largest increase taking place in FY 2016 (total highlighted in red). This increase was partially related to an agency Voluntary Buy Out of approximately 100 employees. However, the non-personnel expenditures decreased $5 million for the audit period. The increase in total expenditures outpaced the increase in total revenues by $2 million ($15 million increase in expenditures - $13 million increase in revenues = $2 million) for the time period of our analysis. The agency was able to sustain the overspending through the funds made available in the Program Funds Recovered (PFR) account. This account is discussed later in the report.

- Four out of the seven years of our analysis on the previous page (FY 2013 through 2016) reflect the fact that agency expenditures exceeded agency revenues. Spending in excess of current year revenues ranged from $1 million in FY 2013 to $16 million in FY 2016. It should be noted that FY 2017 indicated $7 million less in expenditures than current year revenues. However, data from one year is insufficient to determine whether expenditures being less than revenues is a trend or an anomaly.

Budget Analysis
In the previous section, we compared revenues to expenditures on a cash basis. This section includes an analysis of budgeted revenue to actual revenue per budget year (BY) and expenditures per BY for BY 2011 through BY 2017. (Note: "actual" revenues and expenditures are on a budget-year basis. Budget years can be for periods up to thirty months and may overlap multiple fiscal years.)



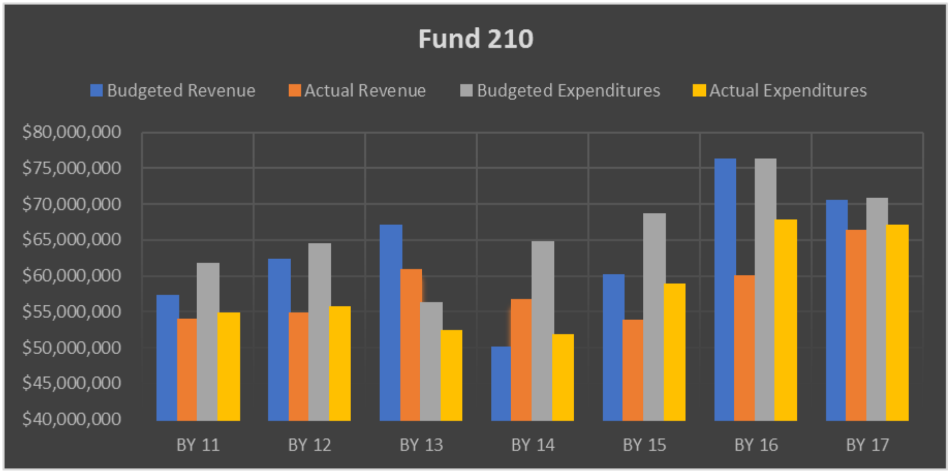
When all funds are considered in the aggregate for our period of analysis (see graph above), two concerning trends are illustrated.

- Apart from BY 2016, budgeted revenues are much higher than the actual revenues received. This supports claims by OSDH employees that senior management (the Senior Deputy Commissioner and the Business Planning Director) "padded" the revenue estimates to justify their expenditure budgets. Revenue budgets/projections do not appear to be based on historical trends.

- Actual expenditures per BY for BY 2012 through BY 2015 exceeded actual revenues per BY. The agency was spending more than it was receiving in revenues annually; this is not a sustainable operating practice.

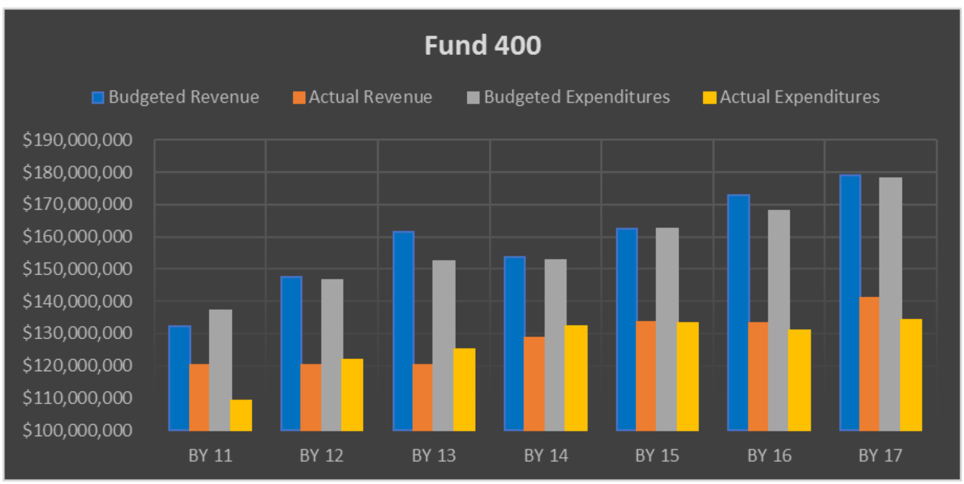
Additional analysis for the Public Health Special Fund (Fund 210)[6] and federal funds (Fund 400) provides further insight.

Public Health Funds (Fund 210)



Fund 210 (Public Health Special Fund) budgeted revenues exceeded actual revenues per budget year in all years but BY 2014. For BY 2013 and BY 2014, actual expenditures per budget year were less than actual revenues for the fund, which is a positive trend. However, starting in BY 2015, this trend reversed and we see actual expenditures outpacing actual revenues, which is not a sustainable operating practice.

Federal Funds (Fund 400)



[6] Fund 210 was created by 63 O.S. § 1-107, which states that the funds "may be budgeted and expended by the Commissioner for the purpose of maintaining and operating the State Department of Health, and in administering and executing the laws pertaining to the duties and functions of the State Department of Health."

A review of the trends for Fund 400 (Federal Funds) indicates that budgeted revenues were consistently much higher than actual revenues for the entire analysis period (see graph on previous page). This is alarming, as federal revenues should be relatively easy to project accurately based on the federal grants the agency has been awarded. Based on interviews with OSDH staff members, Fund 400 was one of the primary funds used by senior management (the Senior Deputy Commissioner and the Business Planning Director) to inflate revenue estimates to justify their expenditure budgets. Budgeted expenditures also appear to have been inflated to levels close to the inflated revenue budgets. Although actual expenditures were closer to actual revenues, grossly inflated revenue and expenditure budgets are misleading and paint an inaccurate picture of available funds.

Overall, inflated and inaccurate budgets do not provide decision-makers within and outside the agency sufficient and appropriate information to make important decisions. Again, expenditures consistently exceeding revenues is not sustainable.

Payroll Expenditure Analysis

We performed additional analyses on payroll expenditures to determine if there were any notable trends of increases or decreases in agency personnel for particular departments or fiscal years. Our analysis revealed the following:

- The agency's authorized number of positions or Full Time Equivalent (FTE) count varied between 2,009 (in FY 2013) and 2,094 (in FY 2017). As of November 6, 2017, the FTE count was 1,996 with 2,049 actual employees. The relationship between the FTE count and the actual number of employees is as follows:

	FY 2011	FY2012	FY2013	FY2014	FY 2015	FY 2016	FY 2017	Nov 6, 2017
FTE	2,069	2,018	2,009	2,010	2,034	2,088	2,094	1,996
Actual	Not Available	2,172	2,071	2,135	2,151	2,227	2,213	2,049

- According to OSDH Human Resources staff, the reason for the actual employee count exceeding the authorized FTE is that there are a number of part-time employees (so two part-time employees equal one FTE).

- We noted one division with a significant increase in personnel, Division 238 – Protective Health Services. This division added a net of 206 personnel during the audit period (307 added – 101 reduced = 206 net); however, this does not factor in any of the employees included in the December 2017 termination of unclassified employees and March 2018 RIF of classified employees.

We also analyzed the data to determine if there were any significant pay increases for particular departments or fiscal years. We defined significant pay raises as any amount **over** $10,000 annually. We identified twelve locations that had 94 significant pay raises between July 1, 2010 and September 30, 2017. The following three divisions[7] accounted for 75 of the 94 pay raises, or 80%:

- 32 significant raises (34%) – Deputy Secretary of HHS/Senior Deputy Commissioner;
- 29 significant raises (31%) – Community & Family Health Services; and
- 14 significant raises (15%) – Commissioner's Office

We reviewed the top nineteen pay raises, which ranged from $30,122 to $41,505 annually, and the Senior Deputy Commissioner's pay raise of $20,500, for proper approval. Proper approval includes an HCM-92 (Employment Action Form) signed by the agency's Cabinet Secretary. The following was noted:

- The pay raise for one individual took effect eight days prior to being properly approved
- The pay raise for the Senior Deputy Commissioner was not properly approved

We noted the following trends in payroll and professional services expenditures (amounts have been rounded):

- Personnel expenditures increased by $31 million (24%) from FY 2012 to FY 2016
- Professional Services expenditures increased by $28 million (89%) from FY 2011 to FY 2016 and decreased by $10 million between FY 2016 and FY 2017

Unsupported $10 million Budget Item

Annual budgets were developed by the OSDH Budget Officer, reviewed by the CFO (if the position was filled), and approved by the Commissioner or the Senior Deputy Commissioner. During the timeframe when the CFO position was unfilled, the budget was reviewed

[7] There was some fluctuation of location codes and divisions during our audit period. However, based on information provided by OSDH management, we estimate the total number of employees for each of these three divisions as follows as of June 30, 2017: Deputy Secretary of HHS/Senior Deputy Commissioner – 118; Community & Family Health Services – 1,558; Commissioner's Office – 23.

by the Business Planning Director and approved by the Senior Deputy Commissioner (the Senior Deputy Commissioner had signature authority for the Commissioner so it is unclear whether he reviewed the budget or not).

According to the Budget Officer, the balanced budgets that were developed and submitted to the Business Planning Director and the Senior Deputy Commissioner were not the same budgets that were submitted to OMES, the legislature, and the Board.

For example, the internal FY 18 budget for the Community and Family Health division indicates a $12 million shortfall (see document below); budgeted expenditures exceed budgeted revenues by $12 million.

Program	SFY 18 Allocation	Payroll	Contractual	Travel	Supplies	Other	Data	Total	Variance
CFHS Admin (IDC) (WA)	350,000.00	348,150.00		2,449.00	440.00	10,804.00	7,499.00	369,342.00	(19,342.00)
CFHS Admin (NON - IDC) (WD)	4,100,000.00	3,615,358.00	8,400.00	76,677.00	1,642.00	277,544.00	120,379.00	4,100,000.00	-
Shared Services (W0)	2,460,482.00	7,261,827.00	530,000.00	91,757.00	655.00	1,323,411.00	1,145,534.00	10,353,184.00	(7,892,702.00)
Nursing Service (WN)	2,060,000.00	1,849,230.00		25,909.00	30,009.00	109,847.00	45,005.00	2,060,000.00	-
Dental Health (QC)	250,000.00	238,777.00		2,000.00	1,700.00	7,033.00	7,752.00	257,262.00	(7,262.00)
Child Adolescent Health (NC)	1,408,144.00	962,404.00	397,274.00	18,165.00			30,301.00	1,408,144.00	-
Peranatal (ND)	4,725.00		2,725.00	2,000.00				4,725.00	-
Infant Mortality (NI)	1,334,000.00	304,869.00	1,012,682.00			5,415.00	11,034.00	1,334,000.00	-
Teen Pregnancy (NK)		288,295.00		8,900.00	2,900.00	7,000.00	10,008.00	317,103.00	(317,103.00)
Maternity (TQ)	25,000.00		25,000.00					25,000.00	-
Family Planning (TS)	2,500,000.00	4,549,655.00		68,250.00	20,000.00		134,423.00	4,772,328.00	(2,272,328.00)
Abstinence (TN)	75,000.00	41,631.00	15,000.00	1,100.00	10,200.00	5,818.00	1,251.00	75,000.00	-
MCH Perinatal (TB)	49,095.00	47,844.00					1,251.00	49,095.00	-
Fetal Infrant (T7)	394,610.00		394,610.00					394,610.00	-
PHEP				14,604.00		27,571.00	26,819.00	68,994.00	(68,994.00)
Violent Death Reporting (5G)		12,366.00					375.00	12,741.00	(12,741.00)
TSET Healthy Living (EK)			-				114,984.00	114,984.00	(114,984.00)
ParentPro (N3)	1,995,921.00	1,575,370.00	313,522.00	26,318.00	1,651.00	23,180.00	55,880.00	1,995,921.00	-
Child Guidance (NG)	2,845,795.00	1,851,918.00	860,000.00	23,879.00	280.00	7,741.00	101,977.00	2,845,795.00	-
Children First (NL)	5,500,000.00	3,032,036.00	2,750,544.00	124,821.00	11.00	72,113.00	140,340.00	6,119,865.00	(619,865.00)
Immunization VFC (P7)		293,908.00		81.00			15,017.00	309,006.00	(309,006.00)
Tuberculosis (PE)		148,420.00	9,293.00					157,713.00	(157,713.00)
Immunization 317 (PG)		379,605.00		9,251.00		561.00	21,588.00	411,005.00	(411,005.00)
Acute Disease (PI)		24,324.00		235.00			1,004.00	25,563.00	(25,563.00)
Senior Companion (W5)							2,502.00	2,502.00	(2,502.00)
Early Foundation (W7)							5,248.00	5,248.00	(5,248.00)
Adult Services (WE)		10,338.00		104.00			2,380.00	12,822.00	(12,822.00)
Child Abuse (WH)	2,214,668.00	147,103.00	2,039,668.00	3,500.00		20,771.00	3,626.00	2,214,668.00	-
Food & Lodging (XK)				-	-	-	2,502.00	2,502.00	(2,502.00)
CHD Communicable Disease (YA)		43,093.00	-				1,871.00	44,964.00	(44,964.00)
Records Management (WC)	1,093,749.00	783,602.00		36,260.00	124.00	109,013.00	164,750.00	1,093,749.00	-
Community Epidemiology (WZ)	81,851.00	71,430.00	5,216.00		542.00	1,538.00	3,125.00	81,851.00	-
Screening & Special Services								-	-
SoonerStart/Early Intervention (VM,YI)		1,763.00		252.00			76.00	2,091.00	(2,091.00)
EPRS (PHEP-CF)	773,902.00	773,902.00						773,902.00	-
TB X-RAY (PI) PE	40,000.00		40,000.00					40,000.00	-
Health Promotion (FE)	281,705.00	217,788.00		2,291.00	13.00	2,268.00	59,345.00	281,705.00	-
Public Health Accreditation (W6)	321,958.00	280,107.00				8,707.00	33,144.00	321,958.00	-
Tobacco (ER)	78,063.00	72,735.00		2,265.00		561.00	2,502.00	78,063.00	-
STD (PK)	376,056.00	353,085.00		5,843.00			19,276.00	378,204.00	(2,148.00)
Federal Medical Asst Percentages (FMAP Match)	1,803,500.00		1,803,500.00					1,803,500.00	-
Total	32,418,224.00	29,580,933.00	10,207,434.00	546,911.00	70,167.00	2,020,896.00	2,292,768.00	44,719,109.00	(12,300,885.00)
Millage	30,737,185.00	29,928,895.00						29,928,895.00	808,290.00

Source: internal budget documents obtained from the OSDH Budget Officer

At the time the budget was presented to the Business Planning Director and the Senior Deputy Commissioner, the intent was for them to decide where to make cuts, or to identify additional revenue sources so projected expenditures would equal projected revenues. During their review, the Business Planning Director and the Senior Deputy Commissioner identified an additional $2 million available in federal funds, reducing the shortfall in the Community and Family Health Budget to $10 million.

All other OSDH budget areas were balanced so when the overall internal OSDH budget was produced, there remained a difference of $10 million between the amount of appropriated funds that were budgeted and the amount of appropriated funds that were actually allocated by the legislature ($63.5 million budgeted and $53.1 million appropriated; see document below).

	Appropriated Funds	Dedicated Funds	Inter-Agency Funds	Other Funds	Total Funds	Actual Appropriation for FY18
State Department of Health						
FY'18 General Revenue Fund for Duties	$63,543,378				$63,543,378	$53,083,790
Kidney Health Revolving Fund 202 for Duties		$0			$0	
Genetic Counseling License Revolving Fund 203 for Duties		$4,650			$4,650	
Tobacco Prevention and Cessation Revolving Fund 204 for Duties		$1,207,393			$1,207,393	
Alternatives to Abortion Services Revolving Fund 207 for Duties		$17,951			$17,951	
Public Health Special Revolving Fund 210 for Duties		$34,804,776	$2,267,800	$30,737,185	$67,809,761	
Nursing Facility Administrative Penalties Fund 211 for Duties		$0			$0	
Home Health Care Revolving Fund 212 for Duties		$310,892			$310,892	
Oklahoma National Background Check Fund 216 for Duties		$1,227,400			$1,227,400	
Civil Monetary Penalty Revolving Fund 220 for Duties		$2,879,776			$2,879,776	
Oklahoma Organ Donor Education and Awareness Program Revolving Fund 222 for Duties		$18,416			$18,416	
Breast Cancer Act Revolving Fund 225 for Duties		$50,000			$50,000	
Sports Eye Safety Program Revolving Fund 226 for Duties		$0			$0	
Oklahoma Leukemia and Lymphoma Revolving Fund 228 for Duties		$50,000			$50,000	
Multiple Sclerosis Society Revolving Fund 229 for Duties		$0			$0	

Source: FY 18 Budget documents obtained from the OSDH Budget Officer

In order to balance the budget, the Business Planning Director and/or the Senior Deputy Commissioner added an additional revenue line titled FY'18 Operational Budget for $10 million (see pink highlight in the document on the next page) and reduced the FY' 18 General Revenue Fund (immediately above the pink highlight) by the corresponding amount. This change was essentially a "plug" to balance the budget.

	Appropriated Funds	Dedicated Funds	Inter-Agency Funds	Other Funds	Total Funds
State Department of Health					
FY'18 General Revenue Fund for Duties	$53,138,108				$53,138,108
FY'18 Operational Budget				$10,459,588	$10,459,588
Kidney Health Revolving Fund 202 for Duties		$0			$0
Genetic Counseling License Revolving Fund 203 for Duties		$4,650			$4,650
Tobacco Prevention and Cessation Revolving Fund 204 for Duties		$1,207,393			$1,207,393
Alternatives to Abortion Services Revolving Fund 207 for Duties		$17,951			$17,951
Public Health Special Revolving Fund 210 for Duties		$34,804,776	$2,267,800	$30,737,185	$67,809,761
Nursing Facility Administrative Penalties Fund 211 for Duties		$0			$0
Home Health Care Revolving Fund 212 for Duties		$310,892			$310,892
Oklahoma National Background Check Fund 216 for Duties		$1,227,400			$1,227,400
Civil Monetary Penalty Revolving Fund 220 for Duties		$2,879,776			$2,879,776
Oklahoma Organ Donor Education and Awareness Program Revolving Fund 222 for Duties		$18,416			$18,416
Breast Cancer Act Revolving Fund 225 for Duties		$50,000			$50,000

Source: FY 18 Budget document obtained from OSDH Budget Officer

Because the budget submission made in the statewide accounting system must match the actual appropriations amount, the Budget Officer stated that they were directed by the Business Planning Director and the Senior Deputy Commissioner to put the extra $10 million into a 400GI fund to "hide" it. Because OSDH could not change the amount of appropriated funds and did not want to add $10 million to a revolving account, the increase was added to the 400GI fund revenue within the budget. Based on comments provided by staff, the GI in 400GI stands for "Gastrointestinal" to reflect what finance department staff thought of the Business Planning Director and Senior Deputy Commissioner's plan.

The Budget Officer's assertions appear to be supported by several e-mails (see next page).

From: [redacted]
Sent: Wednesday, September 13, 2017 5:14 PM
To: [redacted]
Subject: RE: FY'18 Total Budget 82917.xls

Oh yeah! It's in the budget so I suppose it is okay to send however I don't think that fund has cash to support that budget so it needs to be reduced. Further the 228 – leukemia fund was budgeted at $50,000 and was set aside for colorectal cancer. Two problems – 1) we discontinued colorectal cancer screening as part of the budget cuts and 2) we can't use the leukemia money for things other than leukemia.

So in both those cases – 242 and 228 we probably need to do some budget work. That was mostly for you guys to note and correct. We can remove the note and take off the highlight.

[redacted]
Deputy Secretary of Health and Human Services
Sr. Deputy Commissioner

Oklahoma State Department of Health
(405)271-4200
[redacted]

From: [redacted]
Sent: Wednesday, September 13, 2017 5:09 PM
To: [redacted]
Subject: RE: FY'18 Total Budget 82917.xls

[redacted]

Did you want to send with the highlighted line for fund 242 and the note "budget in excess of revenue"?

From: [redacted]
Sent: Wednesday, September 13, 2017 5:04 PM
To: [redacted]
Subject: FY'18 Total Budget 82917.xls

Okay, let's think about it this way. The internal 198GI budgets shouldn't be in the top line because it is not a state appropriated budget. So, I created another line that is just SFY '18 operational budget and copied the amount into "other" just like it was shown in the top line.

The reality is when we took down the WO we probably didn't have to change the fund number we just needed to associate the expense with the appropriate service chief code… anyway, water under the bridge now. If we get a call (and we might very well get a call) we will just tell them we are projecting less revenue than we have to support the current budget and have isolated the amount so we can reduce expenses and (ultimately) the budget.

So… in other words your 198GI is in the second line.

Seem reasonable?

It is apparent that both the Business Planning Director and the Senior Deputy Commissioner were aware of the fact that the budget was not supported by revenue. They also concurred on the decision to insert a plug into the OSDH internal budget spreadsheet, by moving the unsupported $10 million in expenditures to the Fund 400 budget, to obscure the fact that projected revenues were $10 million short of supporting the proposed budget. Although the email above references 198GI, the funds were budgeted in Fund 400 in the final budget submitted to OMES and the Legislature (this reflects $53 million budgeted from Fund 198 and the $10 million included in the Fund 400 budget of $175 million). This essentially further inflated the Fund 400 budget. It should be noted that although this is a readily identifiable example, inflating the Fund 400 budget was a historical trend and not an isolated event (see Fund 400 analysis on page 14). In addition, the agency has historically relied on the use of PFR funds (see page 35) to facilitate the practice of inflating the Fund 400 budget.

Contracts

Contracts with Tobacco Settlement Endowment Trust (TSET) and Oklahoma University Health Sciences Center (OUHSC)

During our initial interviews with current and previous OSDH employees, we were made aware of concerns regarding two contracts. These concerns were also specifically identified by the agency's CFO in his updated response to a SAS 99[8] interview conducted by the State Auditor & Inspector's (SA&I) office as part of the State CAFR audit.

One contract was executed in May 2011 for $3.5 million (a modification was made in December 2011 for an additional $5 million) between OSDH and the TSET to develop a Certified Healthy Community Grant Program and a Certified Healthy Schools Program, consistent with the Certified Healthy Communities standards. The grant program was designed to provide incentives for organizing, implementing policy initiatives, and developing community partnerships that address identified local health issues.

The second contract was executed in October 2011 for $1.5 million between OSDH and OUHSC. The purpose of this contract was to develop an education and training program to recruit, educate, and train racial and ethnic minority students in public health in order to support a public health workforce that adequately represents the diversity of the citizens of Oklahoma.

These contracts came to the attention of the CFO in July 2017, at a time agency management believed OSDH to be experiencing a cashflow crisis. This stemmed in part from the depletion of Ryan White HIV/AIDS Program[9] rebate funds and the agency's perceived inability to pay program-related invoices and make payroll (these issues are discussed in other sections of this report).

The following email between the Senior Deputy Commissioner and Chief Operating Officer (COO) highlight this issue (see next page):

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[8] **Statement on Auditing Standards No. 99: Consideration of Fraud in a Financial Statement Audit**, commonly abbreviated as **SAS 99**, was an auditing statement issued by the Auditing Standards Board of the American Institute of Certified Public Accountants (AICPA) in October 2002, now part of SAS 122, which requires, among other things, inquiries of management and others within the audited entity regarding the risk of fraud.

[9] The Ryan White HIV/AIDS Program is a federal program that provides a comprehensive system of care that includes primary medical care and essential support services for people living with HIV who are uninsured or underinsured. Although the rebate funds are not technically considered federal funds, they are subject to federal restrictions regarding their use.

From: [redacted]
Sent: Thursday, July 27, 2017 3:44 PM
To: [redacted]
Subject: RE: Budget Watch

Thanks. Nice to talk with [redacted] about communication but she won't have the solution (obviously).

Time to talk about draw procedures and borrows.

I will have a cash transfer amount back from TSET tomorrow. Its in the millions.

[redacted]

[redacted]
Deputy Secretary of Health and Human Services
Sr. Deputy Commissioner
Oklahoma State Department of Health
(405)271-4200
[redacted]

From: [redacted]
Sent: Thursday, July 27, 2017 3:34 PM
To: [redacted]
Subject: RE: Budget Watch

There are other concerns coming from this. [redacted] requested payment of $600k from the Ryan White funds to pay a vendor. There is $15 dollars in the Ryan White fund at OMES. [redacted] is demanding an explanation. I am trying to get hold of [redacted] so we can work through her and keep this off the email chain. We cannot answer the question of when the $3.1 million can be paid back into the fund.

Oklahoma State Department of Health
[redacted]
Chief Operating Officer
1000 NE 10th Street, Suite 310
Oklahoma City, Oklahoma 73117-1299

Of specific concern to the CFO was the fact that the Senior Deputy Commissioner had the ability to obtain millions of dollars at her discretion. He also mentioned concerns about the Business Planning Director creating a "pro forma" invoice, after the fact, for the funds returned from TSET (see email below).

From: [redacted]
Sent: Tuesday, August 08, 2017 9:11 AM
To: [redacted]
Cc: [redacted]
Subject: RE: Reverse Cash Transfer

I just spoke with TSET to check on the transfer, she requested the transfer last Friday however OMES will not have the cash until tomorrow. TSET has also requested an invoice which I am creating now unless you have a template you can send me to utilize and send to TSET. It will need to contain the funding information for deposit. Do you have a draft invoice?

Thanks

The CFO had additional concerns: a total of $8.5 million (TSET) and $1.5 million (OUHSC) having been advanced to the recipients prior to receipt of contracted services, potential lack of contract monitoring, possible related party transactions, and federal funds having been used to pay part or all of the cash advances. We obtained and reviewed relevant documentation related to each contract and created a timeline of events.

On August 16, 2017, the OSDH Chief of Internal Audit and Director of the Office of Accountability Systems requested an opinion from the SA&I Director of Audits, State Agency Audit Division regarding the advancement of funds related to the OSDH contract with TSET. SA&I's response indicated that it was inappropriate for OSDH to advance funds to TSET according to 74 OS § 85.44(B), which states in part:

> *Payments for products or services pursuant to a contract executed by a state agency, whether or not such agency is subject to the Oklahoma Central Purchasing Act, Sect 85.1 et seq. of this title, shall be made only after products have been provided or services rendered.*

After reviewing the contracts and supporting documentation, we affirm the previous opinion and guidance provided by our office on this issue stating that the advancement of funds from OSDH to TSET is not an allowable practice based on state law. It is our opinion that this also applies to the contract between OSDH and OUHSC which was very similar in nature to the contract with TSET. The Oklahoma State Constitution, Article 10 § 15.A also states:

> *Except as provided by this section, the credit of the State shall not be given, pledged, or loaned to any individual, company, corporation, or association, municipality, or political subdivision of the State, nor shall the State become an owner or stockholder in, nor make donation by gift, subscription to stock, by tax, or otherwise, to any company, association, or corporation.*

In addition, $7.5 million of the $8.5 million total advanced to TSET was paid from 400 funds and all of the $1.5 million paid to OUHSC was paid from 400 funds. These 400 funds are designated as "federal" funds in the statewide accounting system, and in most cases in FISCAL.

Advancing federal funds to a contractor prior to receiving goods or services is not consistent with federal grant management requirements or federal law (2 CFR § 200.305) which in general state that cost reimbursement is the preferred funding method for federal grants. Cash advances of federal funds are rare, are typically to non-federal recipients or sub-recipients (rather than vendors or contractors), are determined allowable on a grant-specific basis, and always require that the recipient minimize the time elapsing between the receipt and disbursement of federal funds.

Because the funds advanced to TSET and OUHSC were paid from OSDH's PFR account (discussed in detail on page 35), it appears those funds were not truly federal in nature but were funds reimbursed for previous expenditures paid from state appropriated or revolving funds. However, the payments were made from Fund 400 in the statewide accounting system, which, although not segregated by federal program, is clearly identified as federal funds. The agency's accounting for federal reimbursements are concerning, but we have no evidence that federal funds were used inappropriately.

An additional funding issue was noted where the authorizing legislation for the TSET program (HB 2774 (2010), § 3.K) stipulates that OSDH may provide a monetary reward to schools that earn certification under the Oklahoma Healthy Schools Act "subject to available funding specifically appropriated for this purpose." Based on the information above, OSDH did not use funds specifically appropriated for this purpose for payments to TSET (which TSET used in part to pay certification rewards to schools) but instead primarily used PFR funds to fund the contracts. This does not comply with the statutory requirements.

In order to gain a better understanding of the two contracts, we interviewed the following individuals:

- Secretary to the Board, who was listed as the contract monitor for both contracts
- Director of the OSDH Center for the Advancement of Wellness
- OSDH Contracting and Acquisitions Agent III who is listed as the buyer on both contracts

Although the general counsel is listed on the OUHSC FY 2015 contract renewal, we were unable to interview him because his employment was terminated prior to our official engagement on this audit.

The Secretary to the Board, who characterized her involvement as purely "administrative," provided one email with supporting documentation where she had requested expenditure reconciliations from TSET for the first two years of the contract. The reconciliations were extremely late; the contract states they were due within 30 days of the end of the preceding contract period, and the one example we were given shows the reconciliations for FY 2012 and FY 2013 were not submitted until February of 2014.

We were unable to determine from the documentation if any significant review or discussion of the reconciliations provided by TSET had been performed. The Secretary to the Board specifically indicated that she believed the Contracting and Acquisitions Agent III or Director of Procurement would have been responsible for contract monitoring.
The Contracting and Acquisitions Agent III confirmed that her role with the TSET and OUHSC contracts was limited to setting up the purchase orders and contracts and processing any renewals, amendments, or modifications to the contract, and that contract monitoring functions should have been performed in the program areas. She expressed her

opinion that significant turnover in the agency has resulted in a lack of training for contract monitors.

The Director of the OSDH Center for the Advancement of Wellness had no knowledge of the contract between OSDH and TSET when she was hired into her position and assumed the program was a TSET program (i.e. funded with TSET funds). She added that there were no contract monitoring files (or any files for that matter) in her area.

Overall, we found no evidence of substantive contract monitoring for either contract by OSDH personnel.

Board

We learned during interviews with the Board President, Board Vice-President (Chair of Audit, Ethics, and Accountability Committee), and a Board member (Chair of Finance Committee) that they became aware of the contracts between OSDH and TSET, and OSDH and OUHSC, during an October 18, 2017 meeting with the CFO, COO, and internal auditor.

The consensus was that they were shocked the agency was "giving" money to TSET or OUHSC, as neither entity appeared to need the money. They were also concerned with the concept of advancing funds. One Board member commented that TSET was a valuable strategic partner but that didn't justify giving them funds. Another Board member mentioned that the rationale for the contract with TSET might have been that they were in a better position to perform some of the "prevention" activities than OSDH.

OSDH Internal Audit

In order to determine if the advanced funds were expended according to the contract, we first interviewed OSDH internal audit staff and obtained their audit workpapers related to the contract between OSDH and TSET. Although not complete, their efforts included obtaining expenditure reports from TSET, working to validate expenditures using OpenBooks on www.ok.gov, and performing an analysis of various aspects of the contract.

It should be noted that the internal audit of TSET was discontinued prior to completion at the direction of the OSDH Interim Commissioner. This also coincided with efforts to terminate the Director of Internal Audits.

Based on our review of their workpapers, we noted the following:

- OSDH internal auditors believe the advancement of funds to TSET to be contrary to state law.

- OSDH internal auditors believe the programs managed by TSET are consistent with the contract.
- OSDH internal auditors reconciled salary amounts between TSET and OMES.

TSET

To determine whether expenditures were in compliance with the contract, we first reconciled expenditures reported by TSET to the statewide accounting system records. TSET spent funds on the following categories and in the following amounts, as of January 20, 2018.

Program Manager Salary	613,913.64
Program Manager Fringe	279,103.31
Total Personnel	**893,016.95**
Evaluation Support	265,499.32
Communications Support	383,345.13
Sub total Personnel and Support	**1,541,861.40**
Admin Fee at 10%	154,186.14
Total Program Support	**1,696,047.54**
Direct Awards	3,146,750.00
Total Expenditures	**4,842,797.54**

8,500,000.00	Total Advanced to TSET (May and December 2011)
(4,842,797.54)	Expenditures from Funds (May 2011 - August 2017)
(3,000,000.00)	Returned to OSDH (August 2017)
657,202.46	**Remaining Funds**

Overall, expenditures by TSET appear to be consistent with the categories of expenditures outlined in the original contract between OSDH and TSET. However, the amounts listed in the itemized budget (included as an appendix to the contract) only cover the original $3.5 million advanced for Certified Healthy Communities and do not include the additional $5 million contract modification to include Certified Healthy Schools. Therefore, we were unable to compare actual amounts expended in each category to an approved budget.

The original contract stated that the contract period was for one year with two additional one-year renewal options. It also stated that cash balances should be refunded to OSDH upon request at the end of each contract year. We obtained detailed evidence of one contract renewal for the first renewal period of May 16, 2012 through May 15, 2013 and limited documentation of a renewal for the period of May 16, 2013 through May 15, 2014. Without a documented contract renewal, all remaining funds should have been returned to OSDH in May 2014. Funds were not returned until August 2017, when OSDH requested them.

On August 8, 2017, a letter was sent from OSDH to TSET requesting the return of $3,000,000. These funds were returned to OSDH as evidenced by the following receipt:

Oklahoma State Department of Health
Accounting Services
Customer Receipt

Receipt Number: 3967197

#00016941

For Monies Received From Mr./Ms. Tobacco Se Inv#TSET2018Special V 8/14/2017

In the Sum of Three million dollars and 00/100 $3,000,000.00

For Services Provided For:
Misc Wire Transfers
210HAX8 001810ZZ00 10001 5810101
Method of Payment: Other

E. Krogstad
Received By:

THIS RECEIPT DOES NOT CONSTITUTE A LICENSE WITHIN THE STATE OF OKLAHOMA

In addition, TSET was continuing to expend funds without a valid contract renewal in place from May 2014 until a Memorandum of Understanding was executed in September of 2017. This memorandum allowed TSET to "provide support for the work being completed pursuant to the Contract and Purchase Order, as amended, until June 29, 2018" and "to work with OMES and the OSDH for the remittance of any remaining funds left from the original $8,500,000 after the work and terms of the Contract and Purchase Order, as amended, has concluded."

On November 9, 2017, the Interim Commissioner sent a letter to TSET requesting the return of all remaining funds at the time of the accounting report provided by TSET to OSDH ($1,464, 036). A response was sent to OSDH from TSET on November 15, 2017 disputing the amount to be returned and some of the key points of the November 9th letter. However, TSET indicated their willingness to work with OSDH to return remaining funds. At the time of our interview of TSET officials on January 12, 2018, we were informed that TSET, at the advice of their general counsel, had requested and was waiting on a "proper invoice" from OSDH for the return of remaining funds.

<u>OUHSC</u>

To determine whether expenditures complied with the contract, we obtained the expenditure reports provided by OUHSC to OSDH. Based on our review of those reports, it appears OUHSC spent funds on the following summarized categories and in the following amounts, as of September 20, 2017 (see next page):

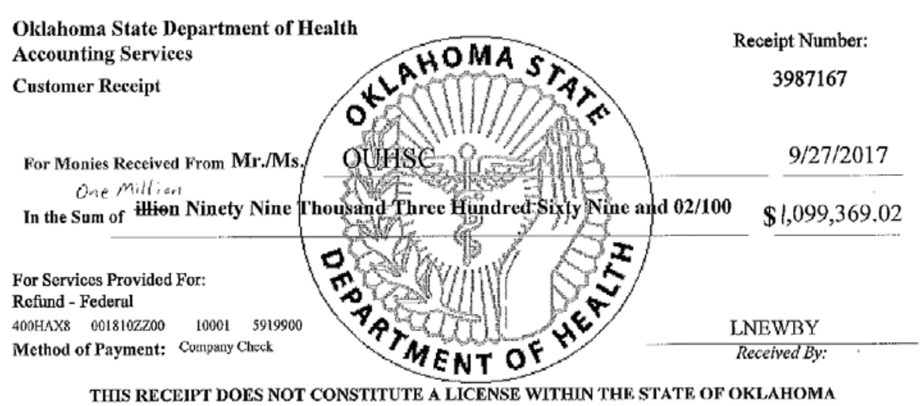
Operating Costs	129,330.83
Student Support	271,300.15
Total Expenditures	**400,630.98**

1,500,000.00	Total Advanced to OUHSC (October 2011)
(400,630.98)	Expenditures from Funds (October 2011 - September 2017)
(1,099,369.02)	Returned to OSDH (September 2017)
0.00	**Remaining Funds**

Overall, expenditures by OUHSC appear to be consistent with the categories of expenditures provided for in the original contract between OSDH and OUHSC.

We also obtained a copy of the "Attachment B" Workplan (required by the original contract) and a program participant list from OUHSC. The workplan appears to be consistent with the contract requirements. To confirm that all employees listed were hired into full-time positions with OSDH in accordance with the contract and workplan requirements, we traced the individuals listed on the program participant list to personnel records in the statewide accounting system.

We reviewed evidence of contract renewals for FY 2012, FY 2013, FY 2014, and a new contract for FY 2015 (with four 1-year renewal options). We reviewed evidence of contract renewals for FY 2016 and FY 2017. A letter was sent to OUHSC on September 17, 2017 notifying them that that the contract was being terminated and requesting return of $1,099,369.02. These funds were returned to OSDH as evidenced by the following receipt:


Oklahoma State Department of Health
Accounting Services
Customer Receipt

Receipt Number: 3987167

For Monies Received From Mr./Ms. OUHSC 9/27/2017

In the Sum of One Million ~~illion~~ Ninety Nine Thousand Three Hundred Sixty Nine and 02/100 $1,099,369.02

For Services Provided For:
Refund - Federal
400HAX8 001810ZZ00 10001 5919900
Method of Payment: Company Check

LNEWBY
Received By:

THIS RECEIPT DOES NOT CONSTITUTE A LICENSE WITHIN THE STATE OF OKLAHOMA

Contract with OMES for CORE Phase II Implementation

In 2011, OSDH began working with the OMES Information Services Division (ISD) to move away from their duplicative internal accounting system known as FISCAL (see next section in this report) and to integrate all accounting functions into the statewide accounting system. This project was known as "CORE Phase II Implementation."

OMES ISD sub-contracted with two vendors, CherryRoad Technologies and Local People, to complete this project. Each vendor was contractually required to provide progress reports on a regularly scheduled basis and was covered by the following Statements of Work (SOW) as appendices to the contracts between OSDH and OMES ISD with specific deliverables (tasks) due by certain dates.

CherryRoad – SOW #65

5. SOW Tasks

Milestone	Planned Start	Planned Finish
OSDH Project	05/23/2012	06/21/2013
Project Management Phase	05/23/2012	03/27/2013
Initiation Phase	07/9/2012	08/01/2012
Initiation	07/9/2012	08/01/2012
Design Phase	09/11/2012	02/01/2013
Configuration (By Module)	07/7/2012	10/12/2012
Business Process Testing (By Module)	09/11/2012	02/01/2013
Development Phase	07/30/2012	01/03/2013
Modifications	07/9/2012	12/12/2012
Conversions	08/13/2012	01/03/2013
Interfaces	07/9/2012	09/28/2012
Reports	07/9/2012	12/10/2012
Validation Phase	08/01/2012	05/13/2013
End-User Training	08/01/2012	02/14/2013
System Rollout Preparation	12/10/2012	01/11/2013
Testing and Acceptance	01/21/2013	05/06/2013
Perform Integration Test.	01/21/2013	03/22/2013
Perform User Acceptance Test.	03/25/2013	05/03/2013
System Rollout	05/07/2013	05/13/2013
Perform System Rollout	05/07/2013	05/13/2013
DELIVERABLE: GO-LIVE	05/13/2013	05/13/2013
Post Implementation Support Phase	05/14/2013	06/21/2013
Provide on-site Support for six weeks following Go-Live	05/14/2013	06/21/2013

CherryRoad – SOW #74

6. SOW Tasks

Milestone	Planned Start	Planned Finish
Project Initiation	12/12/2011	12/12/2011
Map Current Agency Process for GPC, AR, BI, IN, PO, AM, TL	12/12/2011	2/10/2012
Develop revised process flows	2/3/2012	3/2/2012
Agency Review (Fit Session)	3/5/2012	3/16/2012
Develop 10% Plan	3/19/2012	4/6/2012
Develop Roles and Responsibilities	3/26/2012	4/10/2012
Present 10% Proposal	4/11/2012	4/13/2012

Local People – SOW #11.

5. SOW GPC/ARBI Implementation and Support For:

Development Phase	07/30/2012	01/03/2013
Modifications	07/30/2012	12/12/2012
Conversions	08/13/2012	01/03/2013
Interfaces	08/02/2012	09/28/2012
Reports	08/23/2012	12/10/2012
Validation Phase	08/01/2012	05/13/2013
End-User Training	08/01/2012	02/14/2013
System Rollout Preparation	12/10/2012	01/11/2013
Testing and Acceptance	01/21/2013	05/06/2013
Perform Integration Test.	01/21/2013	03/22/2013
Perform User Acceptance Test.	03/25/2013	05/03/2013
System Rollout	05/07/2013	05/13/2013
Perform System Rollout	05/07/2013	05/13/2013
DELIVERABLE: GO-LIVE	05/13/2013	05/13/2013
Post Implementation Support Phase	05/14/2013	06/21/2013
Provide on-site Support for six weeks following Go-Live	05/14/2013	06/30/2013

On February 27, 2018, we requested information from OMES ISD related to this project/contract including copies of progress reports provided in accordance with the contracts, copies of evidence of completion of tasks, an explanation and comparison of the services provided by Local People compared to what was provided by CherryRoad, and a copy of the project termination letter submitted to OMES ISD by the Senior Deputy Commissioner on October 21, 2013. As of the date of this report, we had not received any of the requested information from OMES ISD.

Executed contracts between OMES ISD and OSDH for this project totaled $3.7 million and the agency spent $3.6 million related to the project, which was never completed. Based on our interviews of a former long-time CFO and the Chief of Accounting Services, the project was a “failure” that OSDH walked away from after being told by OMES ISD that they would need to invest additional millions and the project still wouldn’t meet some of OSDH’s biggest “needs” and requests.

Duplicative Financial System (FISCAL) and Inappropriate Accounting Practices

The introduction to the Statewide Accounting Manual for the State of Oklahoma states, "The state has established a statewide system referred to as the State Accounting System that must be used by all state agencies to record their official financial transactions." This system is the official record of account for all state transactions and includes actual cash balances and transactions for all funds.

One of the challenges in obtaining adequate financial information for decision making is the fact that OSDH has operated with a duplicative internal financial information system known as FISCAL for over thirty years. This system is also supplemented with numerous ancillary Microsoft ACCESS databases. The agency does not maintain a central listing of all the databases being utilized.

Further complicating matters is the fact that many financial staff within OSDH do not recognize the statewide accounting system as the record of account but place more reliance on information produced by FISCAL because of the level of detail that is maintained by that system. This is despite the fact that information obtained from FISCAL often does not reflect actual transactions and balances reported by the statewide accounting system.

The use of this internal system has also resulted in, or at least supported, several unorthodox accounting practices known as Payroll Not Posted (PNP), Borrows (internal within FISCAL), and Program Funds Recovered (PFR), all of which contributed significantly to the agency's perceived financial situation and the decision to request a $30 million emergency supplemental appropriation.

Payroll Not Posted (PNP)

In the statewide accounting system, the payroll is initially paid out of the 400 fund (federal). This action generates a payroll allocation file containing detailed payroll costs that is subsequently posted in FISCAL. This posting process matches payroll expenditures with the appropriate funds.

Any payroll or data expenditure (charges from OMES related to IT services) that fails to post in FISCAL becomes PNP. PNP occurs if there is either insufficient budget or if there is insufficient cash in the appropriate fund in FISCAL. To allow a PNP expenditure to post that previously failed for insufficient budget, the budget either needs to be increased or the expenditure (payroll item) needs to be paid from a different fund that has adequate budget and cash available (in FISCAL).

If PNP occurred due to insufficient cash within FISCAL, the expenditure needs to be paid from a different fund that has adequate budget and cash, or the fund needs to "borrow" cash from another fund. Borrows/loans are made within the same fund type.

Borrows
Borrows are internal movements in FISCAL that occur within the same fund type, i.e. revolving to revolving. Because OSDH operates primarily as a reimbursement agency (they receive reimbursements after incurred expenditures have been paid), in order to initially pay expenditures (typically payroll), the need to "borrow" cash internally occurs routinely.

In FISCAL, when a fund has insufficient cash to pay payroll or cover non-payroll expenses, it "borrows" the amount required so payroll can post or expenses can be paid. It is key to OSDH operations that payroll posts as quickly as possible because the agency will not be able to draw federal funds (be reimbursed) until the payroll has been posted.

The OSDH position is that it requires actual cash to extinguish prior year borrows in FISCAL and that, without a cash infusion, eliminating prior year borrows with current year dollars would leave OSDH unable to continue as a going concern. OSDH does not retain historical borrowing records. Borrows/loans are tracked by spreadsheet and continuously updated as old borrows are paid off and new ones are created.

When a borrow occurs in FISCAL it is simply an internal realignment of agency funds. Repaying a loan that 210X made to 210Y (two areas within the same revolving fund in the statewide accounting system) is basically shifting funds in FISCAL to satisfy detailed internal budget requirements. With very few exceptions, repayment of borrows or corresponding cash infusion is not required. The only type of borrows that would need to be repaid are restricted funds that were loaned out in the statewide accounting system such as Ryan White funds or other funds that have statutory restrictions. As of March 2018, no "borrows" exist in the statewide accounting system requiring repayment of restricted funds.

Cash infusions to close out funds in prior fiscal years in FISCAL should only be required if there is no cash in the corresponding funds in the statewide accounting system and there are either outstanding prior year bills that have not been paid in the statewide accounting system or there are loans made from restricted funds that have not been repaid. Current year borrows (if they have not reduced restricted funds) are purely internal issues and, by themselves, do not require a cash infusion.

Effect of PNP and Borrows
According to OSDH, as of July 12, 2017, PNP totaled $8,959,530, and as of September 20, 2017, "borrows" totaled $21,680,000.

Based on our analysis, "borrows" and PNP are both internal to FISCAL and have *no effect* on actual cash available or cash required in the statewide accounting system. Neither the elimination of PNP nor the repayment of a "borrow" requires actual cash. Even though payroll may not be posted in FISCAL, thus creating PNP, the actual payroll has already been paid; therefore, no additional cash is required to eliminate PNP. A borrow/loan between 400 funds or 210 funds in FISCAL does not change the cash balance in the 400 or 210 fund in the statewide accounting system. There are no actual expenditures (payroll or otherwise) that have not already been paid in the statewide accounting system because of "borrows" or PNP in FISCAL.

Borrows Effect on Restricted (Ryan White) Funds

During July 2017, concerns regarding the fund balance for the Ryan White program were noted by the OSDH finance staff. It was determined that there were insufficient funds to pay an invoice related to the program.

In response to questions from the Health Resources and Services Administration regarding the balance of the fund, OSDH responded January 2, 2018 with the following information. After running payroll on July 14, 2017, the balance in the statewide accounting system 400 fund dropped from $6.2 million to approximately $222,390. According to FISCAL, the balance in the Ryan White fund at this time was $3,261,305.29 and by August 9, 2017, the balance in the statewide accounting system 400 fund was $9,116,558.90.

We confirmed that the balance in the Ryan White fund (according to FISCAL) was $3,261,305.29 on Friday, July 14, 2017 and $3,256,876.18 on Monday, July 17, 2017.

OSDH asserted that the temporary drop in the 400 fund (below the restricted Ryan White fund balance of $3.26 million) was due to a delay in payroll processing caused by the fact that the aforementioned payroll spanned two fiscal years (FY 2017 and FY 2018).

According to the statewide accounting system Summary of Receipts and Disbursement (SRD) reports, cash balances for the 400 fund and the following unrestricted funds (that could have been used to transfer funds into the 400 fund) were as follows:

Month Ended	Fund 400 (Federal)	Fund 197 (Appropriated)	Fund 198 (Appropriated	Fund 210 (Revolving)	Fund 79991 (Clearing Acct.)	**Total**
6/30/2017	$3,764,426	$9,515,608	$ 0	$3,366,327	$3,587,291	**$20,233,651**
7/31/2017	$ 903,782	$6,871,809	$1,423,649	$3,703,434	$2,853,931	**$15,759,605**
8/31/2017	$6,700,430	$3,110,571	$5,302,830	$ 525,683	$7,386,552	**$23,026,066**

By OSDH's own admission, the funds in the 400 fund dropped below the required restricted funds of $3.26 million after the July 14, 2017 payroll was paid out of the 400 fund. As per OSDH financial staff, the balance in the 400 fund reached $15 in July 2017. In addition, according to the CFO, OSDH came within one day of defaulting on a $600,000 insurance supplement payment, to be paid with 400 restricted funds, because funds available in the 400 fund were insufficient (only $15 available).

We were only able to determine fund balances at the end of each calendar month (depicted in table above) so we cannot determine the actual 400 fund balance after payroll was run or on the dates leading up to the $600,000 payment. It is clear that the 400 fund was still well below the required $3.26 million on July 31, 2017 when the balance (according to the statewide accounting system *SRD* report) was $903,782. According to the statewide accounting system *Allotment Budget and Available Cash* report there was only $92,559 available on July 31, 2017. However, it appears that there were ample unrestricted funds available to replenish the 400 fund throughout this time period. We were unable to ascertain *why* OSDH failed to replenish the 400 fund in a timely manner when the $600,000 invoice became due.

Program Funds Recovered (PFR)

PFR (400H) is an OSDH-created slush fund that only exists in FISCAL. The PFR fund receives cash from federal reimbursement payments after each individual fund's Time and Effort (T&E) validation if validated costs exceed booked costs. Booked costs are estimated costs based on how each employee is budgeted internally and are the basis for the initial federal draws. Validated costs are actual costs based on what the employee worked on as verified by the T&E process. Historically, validated costs typically exceed booked costs; as a result, excess validated costs (subject to grant limits) are routinely deposited into the PFR account. The PFR account has been the primary source for funds when other federal funds need to "borrow" cash in order to meet obligations.

As a result of this process, reimbursement payments for federal expenditures originally made from the 19X/210 (appropriated and revolving) funds are now retained in the PFR account instead of being returned to the 19X/210 funds. This has the following financial effects:

- Money that should be returned to the 19X/210 funds is now retained in the 400H fund.
    - The 400H funds that should have been returned to 210/revolving funds are not subject to being swept by the legislature (removed for non-OSDH funding purposes)

- Expenditures funded from appropriated and revolving funds are understated and federally funded expenditures are overstated.

There is a PFR equivalent revolving fund (210H) that is used as the funding source for approximately 65% of revolving fund borrows. The 210H fund receives all Vital Records revenue and a 15% administrative fee from any program revenue generated from any source that doesn't already have an indirect cost rate in their contract. The 210H is also funded through portions of payments received by OSDH when they act as a contractor for another entity.

The actual result of this process is that some 19X/210/400 funds that were initially used to pay salary expenditures are retained in the 210H account instead of being returned to the appropriate 19X/210/400 funds. This has the following financial effects:

- Money that should be returned to various 19X/210/400 funds is retained in the 210H fund
- Revolving account funded expenditures may be overstated and appropriated/federally funded expenditures may be understated

We do not believe that the use of either the 400H or 210H PFR funds is appropriate because neither provides an accurate record of OSDH financial transactions for those relying on reports generated from FISCAL. In all circumstances, reimbursements should be returned to the funds from which the payments were originally made.

Because of over-reliance on the duplicative internal financial system, failure to fully consider actual resources available, and the use of unorthodox accounting such as PNP, Borrows, and PFR, OSDH may have significantly overstated the severity of the financial condition of the agency. This ultimately led to the request and receipt of an emergency $30 million supplemental appropriation as defined by HB 1019 (2017 Special Session). It also resulted in the termination of 37 unclassified positions and 161 classified positions, which appears may have been unnecessary and will not result in the cost savings claimed by OSDH. It should be noted that in an interview with the CFO and COO (prior to the resignation of the Commissioner and Senior Deputy Commissioner), both agreed that the cause of the "current financial situation" was a result of internal borrows and internal payroll not posted. The CFO explicitly stated that he estimated it would take approximately $30 million to cover the agency's current borrows and PNP.

In the corrective action report submitted to the Oklahoma Legislature as required by HB 1028 (2017 Special Session), the interim commissioner stated that a "critical infusion of funds in the amount of $30 million . . .

allowed OSDH to stabilize payroll and turn its attention to issues causing the staggering financial crisis in which OSDH finds itself." The corrective action report went on to state that "it became imperative that a supplemental infusion of funding would be necessary to make payroll (approximately $11.6 million)."

This information appears to have been based on data from the internal FISCAL system and does not paint an accurate picture of the agency's true financial condition at the time of the request. We performed an analysis of the cash balances of the agency for the time period of June 2017 through February 2018 (see on page 38). Based on our analysis, at no point during this time period did the "Estimated Available Unrestricted Cash" at month-end fall below $11.5 million.

This contradicts the claim that $11.6 million was "necessary to make payroll." It also contradicts the statement that the agency was in a "staggering financial crisis." By simply transferring funds from their clearing account to agency funds on a more frequent basis (OSDH only transfers once a month), they could have improved their monthly cashflow by at least $3 million. **<u>It appears the agency had sufficient unrestricted cash to make payroll and did not actually need the $30 million supplemental appropriation.</u>**

Fund	Name	30-Jun-17 SRD	31-Jul-17 SRD	31-Aug-17 SRD	30-Sep-17 SRD	31-Oct-17 SRD	30-Nov-17 SRD	31-Dec-17 SRD	31-Jan-18 SRD	28-Feb-18 SRD
194	Appropriated									
195	Appropriated									
196	Appropriated	0	2,400	2,400	2,400	2,400	0	0	0	
197	Appropriated	9,515,068	6,871,810	3,110,572	2,090,969	1,548,976	31,365,315	30,274,193	20,471,415	20,430,329
198	Appropriated		1,423,649	5,302,830	4,838,075	3,409,499	4,331,227	5,391,370	9,334,512	10,407,256
210	Public Health Special	3,366,327	3,706,435	525,683	991,948	1,681,332	754,259	1,293,460	1,895,033	1,107,434
79901	Clearing Account	3,681,095	2,853,932	7,386,553	3,495,679	3,160,630	4,274,541	4,560,889	4,456,277	5,426,982
400	Federal Grants	3,587,292	903,782	6,700,431	12,607,642	9,999,916	14,049,466	6,370,528	11,476,115	11,775,719
	Federal Grant Reductions - Restricted	(4,000,000)	(4,261,305)	(4,000,000)	(6,028,778)	(6,089,742)	(4,843,529)	(3,443,030)	(5,805,607)	(4,417,896)
	Estimated Available Unrestricted Cash	**$ 16,149,782**	**$ 11,500,703**	**$ 23,028,470**	**$ 17,997,937**	**$ 13,713,011**	**$ 49,931,279**	**$ 44,447,410**	**$ 41,827,747**	**$ 44,729,825**
	LESS: $30 MIL SPECIAL APPROPRIATION						**$ (30,000,000)**	**$ (30,000,000)**	**$ (30,000,000)**	**$ (30,000,000)**
	Estimated Available Funds Less Special Approp.						**$ 19,931,279**	**$ 14,447,410**	**$ 11,827,747**	**$ 14,729,825**
202	Kidney Health	1	1	1	1	1	1	1	1	1
203	Genetic Counseling Licensure	31,649	31,665	30,786	31,166	32,382	32,882	33,440	34,619	36,214
204	Tobacco Prevention	956,203	1,017,704	1,042,288	1,104,723	1,107,948	1,215,749	1,292,974	961,048	976,552
207	Alternatives	27,952	27,952	22,952	22,952	22,952	22,952	22,952	22,952	22,952
211	Nursing Facility Admin Penalties	56,471	56,554	56,554	56,554	62,362	62,362	62,362	68,592	68,592
212	Home Health Care	769,319	811,066	818,979	786,684	762,340	747,538	734,336	717,277	695,750
216	National Background Check	1,460,582	1,368,593	1,431,060	1,411,944	1,236,195	1,280,217	1,345,910	1,307,837	1,240,903
220	Civil Monetary Penalties	7,834,076	7,621,513	7,496,104	7,410,991	6,928,736	7,616,354	7,306,825	7,135,968	6,989,778
222	Organ Donor Education	143,938	132,307	136,152	142,034	158,983	176,602	200,687	238,931	247,855
225	Breast Cancer	116,633	117,934	119,236	120,478	122,018	124,038	125,238	126,378	127,558
226	Sports Eye Safety	4,965	5,015	5,030	5,030	5,030	5,030	5,030	5,035	5,040
228	Leukemia & Lymphoma	63,432	63,441	63,441	63,441	63,441	63,441	63,441	63,441	63,443
229	Multiple Sclerosis Society	151	158	158	158	158	158	158	158	163
233	Prevent Birth Defects	2,105	2,125	2,125	2,145	2,165	2,165	2,185	2,185	2,185
235	Oklahoma Lupus	12,513	12,568	12,589	12,589	12,589	12,589	12,589	12,589	12,591
236	Trama Care Assist	2,327,453	3,706,244	3,209,432	3,074,027	2,815,082	1,710,782	1,244,863	1,475,910	2,471,676
242	Pancreatic Cancer Research	11,910	11,980	10,151	8,090	7,272	7,291	7,691	8,171	8,330
250	Regional Guidance Centers	12	12	12	12	12	12	12	12	12
255	Lic Prof Counselors									
265	Child Abuse Prevention	151,777	138,911	135,518	133,227	133,664	133,638	136,527	136,664	140,338
267	Emergency Medical Technician	149,957	150,217	150,317	150,517	150,757	151,057	151,217	151,557	151,757
268	Emergency Response Systems	2,481,827	2,499,570	2,609,367	2,701,641	2,764,616	2,631,995	2,696,444	2,559,892	2,642,376
284	Dental Loan	353,453	312,176	341,682	341,682	297,313	263,957	388,262	405,754	407,215
285	Institute for Disaster & Emergency	1,657	1,657	1,657	1,657	1,657	1,657	1,657	1,657	1,657
290	OK Safe Kids Asso	860	860	860	860	860	860	860	860	860
295	State Athletic Comm	218,549	197,178	254,467	261,785	260,630	266,972	270,424	268,223	291,751
340	CMIA - WIC	22,421	(402,509)	(244,310)	(594,663)	343,514	334,895	(76,371)	235,188	239,831
490	ARRA	156,461	156,461	156,461	156,461	156,461	156,461	156,461	156,461	156,461
700					891,162					
994	Payroll Withholding	4,084	3,744	444	3,598	(715)	(180)	4,957	3,028	2,584
	SUBTOTAL	**$ 17,360,411**	**$ 18,045,099**	**$ 17,863,515**	**$ 18,300,946**	**$ 17,448,423**	**$ 17,021,475**	**$ 16,191,131**	**$ 16,100,388**	**$ 17,004,425**
	TOTAL	**$ 33,510,192**	**$ 29,545,801**	**$ 40,891,985**	**$ 36,298,883**	**$ 31,161,433**	**$ 66,952,754**	**$ 60,638,541**	**$ 57,928,134**	**$ 61,734,250**

Additional analysis of the month-end cash balances indicates that the $30 million emergency special appropriation (which was transferred into fund 197 in November 2017) had not been disbursed as of the end of February 2018. According to the grants reporting officer, $20 million has been used primarily to "pay" internal borrows, prior year payroll not posted, and data bills not posted. He also stated that the remaining $10 million will be used for the same purpose and approximately $3 million of these funds would be used to pay costs associated with the RIF of 161 classified employees and termination of 37 unclassified employees. <u>Therefore, because payroll and data expenditures **have already been paid by OSDH in the statewide accounting system,** what is *really* occurring within FISCAL is an internal realignment of funds that have little or no bearing on actual OSDH statewide accounting system accounts.</u>

Additionally, the savings projected by the agency related to the elimination of 198 employees is not accurate. The following table is the agency's projected cost savings reported in the corrective action report to the Oklahoma Legislature:

Table 1: Cost Saving Measures and Anticipated Results

Cost Saving Measure	Projected Savings SFY 2018	Projected Savings SFY 2019
Furlough	$1,235,916	N/A
RIF - Unclassified*	$1,281,252	$2,562,505
RIF - Classified*	$1,281,252	$7,550,147
999 Employees	$92,400	$140,000
Staff to County Millage	$1,254,000	N/A
GALT Contract	$1,980,000	$3,000,000
TSET Contract	$3,000,000	N/A
College of Public Health Contract	$1,000,000	N/A
OCAP Contracts Termination	$928,000	$1,600,000
FQHC Contracts Termination	$1,102,000	$1,900,000
Fleet Utilization	$320,000	$640,000
Shipping Program Products	$60,000	$60,000
Cell Phone / Hot Spot Consolidation	$72,300	$96,400
WC Premium Cost Reduction	$266,197	$266,197
Estimated Total Savings	$13,873,317	$17,815,249

Source: OSDH Corrective Action report submitted to the Legislature as required by HB 1028

Based on information in the table above, the agency projects to save over $10 million ($2,562,505 SFY 2019 RIF – Unclassified + $7,550,147 SFY 2019 RIF – Classified = $10,112,652) per year as a result of terminating the 198 employees. This is close to the projected savings reported in the RIF plan ($2,500,000 for unclassified employees + $8,000,000 for classified employees = $10,500,000 total savings) submitted to OMES on December 6, 2017. However, these savings appear to be significantly overstated.

We obtained the data from OSDH used to prepare the cost and savings estimates related to the termination of the 37 unclassified employees and RIF of the 161 classified employees. We recalculated their projected cost savings for unclassified employees using the same data that OSDH had used. We determined that the projected annual savings for terminated unclassified positions appeared to be accurate within approximately $100,000. We recalculated their projected cost savings for classified employees using the same data that OSDH had used. Our calculation is as follows:

	Salary (Full-Time Annual Rate)	Insurance Premiums (2017 data)	Longevity bonus w/FICA	Total Savings
Annual Savings	$5,957,420	$1,093,726	$171,087	$7,222,233

Based on our calculation, it appears that at a minimum, OSDH overstated projected savings by over $777,000 ($8,000,000 - $7,222,233).

Upon further analysis, we determined that the agency did not use a consistent methodology to calculate the cost savings for the RIF – Classified Employees. Specifically, although payroll funding source was considered for the unclassified positions to be terminated, it was not for the classified positions included in the RIF. Eliminating positions that are funded with federal or millage funds does not result in a cost savings to the agency unless those funds can be shifted to remaining employees. The cost savings figure used for the classified positions essentially assumes that all related payroll costs were paid from appropriated or revolving funds and would therefore result in cost savings.

If we were to use the same methodology for calculating savings resulting from the classified RIF as OSDH used to determine savings from the termination of unclassified positions, the results would be as follows:

	Non-Federal Non-Medicaid Non-Millage Salary	Insurance Premiums (2017 data)	Longevity bonus w/FICA	Total Savings
Annual Savings	$2,770,159	$508,575	$86,059	$3,364,793

If one were to assume that positions funded by millage would not result in the loss of the millage, the results would be as follows:

	Non-Federal Non-Medicaid Salary	Insurance Premiums (2017 data)	Longevity bonus w/FICA	Total Savings
Annual Savings	$5,033,168	$924,042	$146,430	$6,103,640

Based on the information presented above, the cost savings related to the RIF were overstated by approximately $2 million ($8 million -$6 million) and potentially up to $5 million ($8 million - $3 million). This is worsened by the fact that as a condition to receiving the $30 million supplemental appropriation, HB 1028 requires a 15% reduction in state appropriations by June 30, 2019. This amounts to approximately $8 million ($53 million FY 17 appropriation X 15%) which the agency claimed to be saving at least in part with the RIF. Had the agency not requested the $30 million, there would have been no House Bill 1028 requiring a 15% cut in state appropriations. Consequently, many of the personnel cuts may not have been necessary either.

Subsequent to our fieldwork, we obtained additional information from an OSDH regional director regarding concerns about the RIF plan. His concerns had previously been communicated to the Senior Deputy Commissioner, CFO, COO, and the Deputy Commissioner and the Assistant Deputy Commissioner for the Community and Family Health Services Division in October 2017 and the Interim Commissioner in November 2017. Included in those communications were concerns about the accuracy of the cost savings calculations, specifically including the central office's failure to consider funding sources for employees being terminated. As previously noted, failure to consider employee funding sources could significantly impact the actual cost savings realized by the agency. As indicated by the regional director in his communications to senior management, the proposed RIF of 23 employees with an annual payroll of $1,720,000 would only result in a net savings of $300,000 in state appropriated dollars. This is less than 18% of the total payroll amount for those 23 employees. The response received by the regional director from the central office was that it was also a cashflow issue because of their process of fronting payroll costs and seeking reimbursements.

According to the regional director, the cashflow issue was made worse by a historical lack of timely invoicing for payroll costs by the central office (often two months late). Timely billing could significantly improve agency cashflow issues with reimbursements from county millage funds. The information we obtained from the regional director corroborates our findings related to the RIF cost savings calculations and confirms that OSDH executive management was aware of, but chose to ignore, potential problems with their calculations prior to reporting projected cost savings to the legislature and terminating 198 OSDH employees.

Recommendations

1. The Board and the Commissioner should recognize the risks associated with this type of environment and work towards evaluating and addressing the situation to ensure the mission of the agency is accomplished in the most efficient and positive manner possible. In addition, they should be cognizant of the risk associated with ineffective communication within the agency and work to eliminate any such barriers in an impartial manner.

   We further recommend management perform some level of continuous monitoring, communicate its expectations for internal controls to all employees, and establish a system of clear communication that relays information from the bottom of the organization to the top and vice versa. The tone at the top regarding internal controls will determine to a great extent the success of the various elements of the internal control framework.

2. OSDH should hire a CFO and Controller with adequate experience in state government including experience with federal grant reporting and experience with the statewide accounting system. The CFO should have unfettered access to, and regular communication with, the Board regarding the financial condition of the agency.

3. OSDH should begin working immediately towards eliminating the duplicative internal accounting system FISCAL, and any related processes that duplicate accounting transactions, and move towards integrating with the statewide accounting system. This may require an agency-wide survey of what end financial information is **<u>needed</u>**, the basis for that need, and the most efficient means of obtaining that information without duplicating efforts. Doing this would eliminate the unorthodox accounting practices of borrows, payroll not posted, and program funds recovered.

4. To maximize cash flow, OSDH should consider transferring funds from the clearing account to agency funds on a basis that is more frequent than once a month.

5. A separate restricted fund should be established at OMES for the Ryan White program rebates. A separate 4XX fund should be established at OMES for any federal grants that may require OSDH to maintain a cash balance.

6. OSDH should begin preparing budgets that reflect reasonable revenue projections based on currently known and historical information. Budgeted expenditures should also reflect estimated available funds and should avoid the use of “plugs” in the Fund 400 to make the budget balance.

7. OSDH should monitor expenditures to ensure that they do not exceed actual revenues during any year as this is not a sustainable operating process.

8. OSDH should work towards a process to pay payroll from an appropriate fund, based on accurate budgets, when it is initially processed in the statewide accounting system rather

than funding all payroll from Fund 400 and then relying on manual entries to correct payroll.

9. OSDH should perform a work-flow analysis of financial staff to determine what tasks they are performing, whether those tasks add value to the financial reporting and accounting process, and if not, how those employee's duties should be re-directed to support the needs of the agency.

10. The OSDH Board should work towards fulfilling their fiduciary responsibilities for the agency as outlined in state statutes and best practices. They should develop a direct line of communication with the new CFO to ensure they receive sufficient and appropriate detailed financial information to perform their duties. When the duties and powers of the Board are transferred to the State Commissioner of Health in January 2019 as outlined in HB 3036, the Commissioner can benefit from following this same recommendation.

11. The Oklahoma Legislature may want to consider recalling all or part of the $30 million emergency special appropriation as the majority of those funds have not been used to pay actual expenses of the agency as of the time of this report.

12. OSDH should implement procedures to ensure timely invoicing of payroll cost by the central office for employees located in county health departments and who are funded by county millage. This process could significantly improve agency cashflow.

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