New Jersey State Legislature
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Department of Human Services
Division of Mental Health Services
Community Services - Grants-In-Aid

July 1, 1996 to October 31, 1998

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State Auditor
The Honorable Christine Todd Whitman  
Governor of New Jersey

The Honorable Donald T. DiFrancesco  
President of the Senate

The Honorable Jack Collins  
Speaker of the General Assembly

Mr. Albert Porroni  
Executive Director  
Office of Legislative Services

Enclosed is our report on the audit of the Department of Human Services, Division of Mental Health Services, Community Services - Grants-In-Aid for the period July 1, 1996 to October 31, 1998.

If you would like a personal briefing, please call me at (609) 292-3700.

Thomas R. Meseroll  
Technical Director  
December 23, 1998
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Department of Human Services  
Division of Mental Health Services  
Community Services - Grants-In-Aid

Scope

We have completed an audit of the Department of Human Services, Division of Mental Health Services, Community Services - Grants-In-Aid for the period July 1, 1996 to October 31, 1998. Our audit included financial activities accounted for in the state’s General Fund.

Annual expenditures of community services were approximately $180 million. Community services carries out the responsibility for general support of outpatient clinics and the planning for a statewide network of community mental health services. The division also contracts with community agencies to provide alternatives to hospitalization, particularly services designed to return the patient to the community and to provide screening services which reduce inappropriate admissions to state and county psychiatric hospitals.

Objectives

The objectives of our audit were to determine whether financial transactions were related to community services, were reasonable and were recorded properly in the accounting systems. We also tested for resolution of significant conditions related to community services in our prior report.

This audit was conducted pursuant to the State Auditor’s responsibilities as set forth in Article VII, Section 1, Paragraph 6 of the State Constitution and Title 52 of the New Jersey Statutes.

Methodology

Our audit was conducted in accordance with Government Auditing Standards, issued by the Comptroller General of the United States.

In preparation for our testing, we studied legislation, administrative code, circular letters promulgated by the State Comptroller, and policies of the Department
of Human Services. Provisions that we considered significant were documented and compliance with those requirements was verified by interview and observation and through our samples of financial transactions. We also read the budget message, reviewed financial trends, and interviewed agency personnel to obtain an understanding of the programs and internal controls.

A nonstatistical sampling approach was used. Our samples of financial transactions were designed to provide conclusions about the validity of transactions as well as internal control and compliance attributes. Sample transactions were judgmentally selected. We also performed site reviews of three providers to interview management and test support for financial and level of service reports.

To ascertain the status of findings included in our prior report and related to our current scope, we identified corrective action, if any, taken by the division and walked through the system to determine if the corrective action was effective.

**Conclusions**

We found that the financial transactions included in our testing were related to the community services, were reasonable and were recorded properly in the accounting systems. In making this determination, we noted certain internal control weaknesses and matters of compliance with laws and regulations meriting management’s attention. We also found that the division has resolved the significant conditions noted in our prior report and related to our current scope, except for the issue of contract closeouts. This issue has been updated in this report.
The division’s contract close-outs are not being performed in a timely manner. During our review of the division’s fiscal year 1997 Close-Out Review Schedule, we noted in a sample of ten contracts only one had been closed out by the division’s Administrative Disposition Unit (ADU) as of October 1998. The Close-Out Review Schedule indicated that eight of the nine open contracts had questioned costs stemming from the ADU’s review of the contract’s final report of expenditures.

Upon further review of the preliminary Close-Out Review Schedule, which identified the division’s 207 community care provider contracts with fiscal years ending June 30, 1997 or December 31, 1997, we noted that 62 percent had not been closed out as of October 1998. In addition, the schedule disclosed preliminary estimated questioned costs of $1.5 million for 71 of the 207 contracts. As of October 1998, only 8 of these 71 contracts have had recoveries made or scheduled for amounts totaling $8,900.

As a result, providers with whom the division has continuing contract renewals on an annual basis are currently in the second quarter of their fiscal year 1999 contracts or the final quarter of their calendar year 1998 contracts without resolving the questioned costs identified in the ADU’s review process dating back to the 1997 contract.

According to the division’s management, the Administrative Disposition Unit has experienced personnel changes and shortages throughout 1998. The Department of Human Services’ Information Memorandum P97-1 informed provider agencies and their independent auditors that effective for fiscal years ending June 30, 1997 and thereafter, the audit report due date is 120 days after the end of the fiscal year. This facilitates earlier closeout of outstanding contracts. The division’s Administrative Disposition Unit is responsible for monitoring the timely submission of the independent auditors’ reports. During our review of the audits for contracts that ended during
calendar year 1997, we noted that only 3 of 109 audit reports covering 207 contracts were received timely.

**Recommendation**

We recommend that the division assign sufficient staff to ensure that contract close-out is completed in a timely manner.

**Auditee’s Response**

We agree with the basic facts and recommendation as outlined in the Report. At the same time, however, it is important that the preliminary questioned costs not be misinterpreted as to the likely potential financial consequences of the current backlog. In this regard, while the "Close Out Review Schedule" does, in fact, include the information as outlined in the Audit Report, it is important to clarify that the "estimated questioned costs of $1.5 million" (of a total of $180 million contracted) were very preliminary results as they represented only the initial efforts of student interns and mathematical computations of differences noted. Moreover, such work had not yet been subject to any level of supervisory review at the time this schedule was provided to the auditors. The schedule itself had been designed as an internal tool by the new supervisor of the Administrative Disposition Unit (ADU) to gauge the extent of preliminary work completed, and to prioritize his efforts to review and finalize such review work.

Experience to date regarding such preliminary questioned costs has shown that, once subject to supervisory review, amounts identified by the student interns are most often drastically reduced. It is also important to note that once all reviews are conducted and reconciled, they account for only a minor percentage of funds recovered because over 90% of all contract recoveries are realized through an initial review of the Final ROE and other review efforts, which usually occur long before the agencies' audit reports are received.

As noted above, a lack of timeliness in receiving the annual agency audit reports within the established guidelines is acknowledged. To address this problem, the Division is revising procedures in this area.
Agencies whose audit reports have not been received by the prescribed deadline will now be notified in writing immediately following the expiration of this deadline. Granting of extensions will require written requests and specific justification, with a withholding of subsequent contract payments when such reports are late.

During the period covered by the audit, the task of closing Marlboro Psychiatric Hospital necessitated the temporary reassignment of certain full-time ADU staff and an over reliance on student interns to focus on this area. Consequently, it is now anticipated that with full-time staff back from their Marlboro closure assignment, they will be able to devote more time to the close-out review process, thus allowing us to decrease our reliance on student interns for such reviews.

Community Service Contracts

According to the division’s Contract Close-Out Guidelines, the Administrative Disposition Unit (ADU) is required to determine if the independent audit report supports the final report of expenditures (ROE). If unexplained material differences exist, a reconciliation must be requested from the contract provider if one was not provided. A review of questioned costs and internal control weaknesses identified by the independent audit report must also be performed by the ADU.

In reviewing the four independent auditors’ reports received in our sample of ten contracts, we noted in three instances, there were material differences between the final ROE and the audited financial statements. These differences ranged from $62,200 to $301,600. Although there may be explanations for these differences, additional investigation is required. Our review of the close-out files for these three contracts indicated that the ADU did not perform the comparison between the auditor’s report and final

The division is not adhering to its Contract Close-Out Guideline procedures.
ROE as required by their procedures. In addition, one of these CPA reports cited four reportable conditions and one material weakness that raised serious questions as to the reliability of the financial records and systems of the provider. The fourth audit report reviewed included numerous contracts with multiple state agencies and did not present, as supplemental data, the required schedule of state and federal financial assistance. Without this schedule, it is difficult, if not impossible, to track whether contract funds were spent.

As a result, the estimates of questioned costs made by the division are based on financial reporting (ROE) by the provider that may be incorrect. Furthermore, the division may not be aware of a provider’s questioned costs and financial problems identified in the independent audit report. Such information is significant in determining both the level of funding and the financial stability of the provider. Additionally, providers with whom the division has continuing contracts in fiscal year 1999 are currently in the second quarter of these contracts. Without having resolved the questioned costs, the division’s current level of funding may not be appropriate.

**Recommendation**

The Administrative Disposition Unit should adhere to the procedures set forth in the division’s Contract Close-Out Guidelines, with particular emphasis on the comparison of the CPA audit report with the provider’s final report of expenditures and the review of questioned costs and internal control weaknesses identified in the CPA report. The ADU should also request a reconciliation from the provider when unexplained material differences exist, as well as a schedule of state and federal assistance if it is not provided.

**Auditee’s Response**

We are in agreement with the first observation and related recommendation regarding the need to adequately reconcile material differences between contract expenditures reported on the agency’s Final Report of Expenditures (ROE) to amounts reported in the agency’s audited financial statements. While
reconciliations may not be cost effective for a limited number of provider agencies, such as county operated facilities or those heavily subsidized by community hospitals, a policy is being developed which will result in identifying those agencies for which a reconciliation will be necessary and assuring that such reconciliations are received in a timely manner. Our own internal close-out review program is also being revised to re-emphasize the importance of obtaining and reviewing such schedules and the need to document explanations of differences between the audit report and the Final ROE.

Regarding the audit report's conclusion that "the Division may not be aware of a provider's questioned costs or financial problems identified in the independent audit report," it is important to note that the Division does make note of such observations and already had a process of both notifying and following-up with agencies on such findings. Corrective action plans are also requested and reviewed as necessary. This process includes a review step in the Division's existing audit review program as well as reliance on the efforts of the Department of Human Services' Office of Auditing (DHS-OA), regarding evaluation of agency audit reports for compliance with federal, state and DHS requirements, as well as indications of internal control weaknesses and reportable conditions. However, since the DHS-OA now only reviews agency audits for which DHS has federal cognizant agency responsibility, the Division will expand its existing procedures and re-emphasize the need for review by ADU staff and that follow-up action is pursued for any such observations in agency audit reports.

Level of Service Reports

The division monitors the contract level of service delivery through quarterly reports prepared by the providers. These reports provide an aggregate over-
Provider level of service reports are not being verified for accuracy. View of the various services rendered to the division’s clients during the report period. This data is then input by the division’s management information system unit into a computer system which generates the Quarterly Contract Monitoring Report. These reports represent the provider agency’s actual performance which will be measured against their contractual commitment. Based on our review of contract files, we noted that none of these reports are being verified by the program analysts for accuracy.

Recommendation

We recommend that the providers’ level of service reports be subjected to random testing, to ensure the accuracy of the data provided.

Auditee’s Response

We agree with the audit report's observation and recommendation regarding verification of providers' level of service reports and will implement steps accordingly.