



# MICHIGAN

OFFICE OF THE AUDITOR GENERAL

## AUDIT REPORT



THOMAS H. MCTAVISH, C.P.A.  
AUDITOR GENERAL

The auditor general shall conduct post audits of financial transactions and accounts of the state and of all branches, departments, offices, boards, commissions, agencies, authorities and institutions of the state established by this constitution or by law, and performance post audits thereof.

– Article IV, Section 53 of the Michigan Constitution

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Michigan  
*Office of the Auditor General*  
**REPORT SUMMARY**

*Performance Audit*  
*Selected Service-Related Contracts and*  
*Grant Agreements*  
*Department of Community Health (DCH)*

Report Number:  
391-0135-08

Released:  
October 2010

*DCH's delegated purchasing authority allows it to enter into contracts for services costing less than \$25,000 and grant agreements in any amount. DCH program areas develop requests for services; make initial awards; develop contracts and grant agreements, as appropriate; and monitor and evaluate contractor and grantee performance. DCH's Contract Management Section ensures that approvals are secured, funds are available, and other requirements are met. DCH had 1,713 service-related contracts and 2,441 service-related grant agreements totaling \$168.3 million and \$1.3 billion, respectively, that were included within the scope of the audit.*

***Audit Objective:***

To assess the effectiveness of DCH's efforts to ensure that selected service-related contracts and grant agreements contained comprehensive service descriptions, detailed budgets, performance criteria, and monitoring provisions.

***Audit Conclusion:***

We concluded that DCH's efforts to ensure that selected service-related contracts and grant agreements contained comprehensive service descriptions, detailed budgets, performance criteria, and monitoring provisions were moderately effective. We noted two reportable conditions (Findings 1 and 2).

***Reportable Conditions:***

DCH needs to improve its controls for ensuring the sufficient development and timely completion of detailed performance-based service contracts and grant agreements (Finding 1).

DCH did not establish training requirements for or ensure that it provided training to its contract and grant agreement administrators (Finding 2).

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***Audit Objective:***

To assess the effectiveness of DCH's efforts to ensure that it awarded selected service-related contracts and grant agreements on a fair and competitive basis.

***Audit Conclusion:***

We concluded that DCH's efforts to ensure that it awarded selected service-related contracts and grant agreements on a fair and competitive basis were moderately effective. We noted two reportable conditions (Findings 3 and 4).

***Reportable Conditions:***

DCH needs to improve its controls over its contract and grant awarding processes (Finding 3).

DCH did not have effective controls for ensuring that employees involved in the selection, monitoring, and evaluation of contractors and grantees were free of conflicts of interest (Finding 4).

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**Audit Objective:**

To assess the effectiveness of DCH's efforts to monitor and evaluate the performance of selected contractors and grantees.

**Audit Conclusion:**

We concluded that DCH's efforts to monitor and evaluate the performance of selected contractors and grantees were moderately effective. We noted one reportable condition (Finding 5).

**Reportable Condition:**

DCH did not establish sufficient controls to ensure that its contract and grant agreement administrators sufficiently monitored and evaluated DCH's contracts and grant agreements (Finding 5).

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**Agency Response:**

Our audit report contains 5 findings and 5 corresponding recommendations. DCH's preliminary response indicated that it agrees with all 5 recommendations.

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A copy of the full report can be obtained by calling 517.334.8050 or by visiting our Web site at: <http://audgen.michigan.gov>



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October 15, 2010

Ms. Janet Olszewski, Director  
Department of Community Health  
Capitol View Building  
Lansing, Michigan

Dear Ms. Olszewski:

This is our report on the performance audit of Selected Service-Related Contracts and Grant Agreements, Department of Community Health.

This report contains our report summary; description of agency; audit objectives, scope, and methodology and agency responses; comments, findings, recommendations, and agency preliminary responses; and a glossary of acronyms and terms.

Our comments, findings, and recommendations are organized by audit objective. The agency preliminary responses were taken from the agency's responses subsequent to our audit fieldwork. The *Michigan Compiled Laws* and administrative procedures require that the audited agency develop a formal response within 60 days after release of the audit report.

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

AUDITOR GENERAL



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## Description of Agency

The Department of Management and Budget\* (DMB) delegated authority to the Department of Community Health (DCH) to enter into one-time or multi-year contracts\* for most services that are expected to cost less than \$25,000 and for grant agreements\* in any amount. The Contract Management Section (CMS) within DCH's Budget and Contracts Division is broadly responsible for ensuring that all DCH-originated contracts and grant agreements are developed, approved, and processed according to applicable laws, rules, regulations, policies, and procedures. CMS records and monitors the processing of all contracts and grant agreements, excluding those that are paid for through the Medicaid Management Information System (generally payments to Medicaid providers for recipient services), in its Contract Tracking System.

DCH requires individual program areas wanting to enter into contracts or grant agreements to develop and forward written requests for services to CMS. These requests accompany the related budget documents and other information throughout the contracting/granting process and serve as a mechanism for CMS to ensure that all the necessary approvals (both within and outside of DCH) are secured, funds are available, and other requirements are met. DCH program areas are responsible for identifying their individual service-related needs, for developing written requests to acquire the needed services, and for evaluating contractor/grantee bids or proposals for purchases that are within DCH's delegated purchasing authority. Also, the program areas are responsible for making initial awards, for developing comprehensive contracts and grant agreements with well-defined statements of work and performance and reporting requirements, and for monitoring\* and evaluating contractor and grantee performance. Upon request, CMS provides technical assistance and training to the program areas related to these functions. If a requested service is within DCH's delegated purchasing authority, CMS is responsible for ensuring that the resulting contract or grant agreement includes the required standard provisions to protect the interest of the State. If CMS determines that a requested service is not within DCH's delegated purchasing authority, CMS forwards it to DMB for processing.

DCH had 1,713 service-related contracts and 2,441 service-related grant agreements totaling \$168.3 million and \$1.3 billion, respectively, that were active at some time during the period October 1, 2006 through August 14, 2008 and included within the scope of our audit.

\* See glossary at end of report for definition.

## Audit Objectives, Scope, and Methodology and Agency Responses

### Audit Objectives

Our performance audit\* of Selected Service-Related Contracts and Grant Agreements, Department of Community Health (DCH), had the following objectives:

1. To assess the effectiveness\* of DCH's efforts to ensure that selected service-related contracts and grant agreements contained comprehensive service descriptions, detailed budgets, performance criteria, and monitoring provisions.
2. To assess the effectiveness of DCH's efforts to ensure that it awarded selected service-related contracts and grant agreements on a fair and competitive basis.
3. To assess the effectiveness of DCH's efforts to monitor and evaluate the performance of selected contractors and grantees.

### Audit Scope

Our audit scope was to examine the records and processes related to selected Department of Community Health service-related contracts and grant agreements. We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives. Our audit procedures, conducted from April 2008 through August 2008 and May 2009 through April 2010, covered selected contracts and grant agreements active at any time during the period October 1, 2006 through August 14, 2008.

Included within the scope of our audit were 1,713 service-related contracts and 2,441 service-related grant agreements totaling \$168.3 million and \$1.3 billion, respectively. Not included within these totals or within the scope of this audit were grant agreements with or related to community mental health organizations, local health departments, and the Temporary Assistance to Needy Families Program. Also excluded were contracts with Medicaid health maintenance organizations, contracts for the purchase of

\* See glossary at end of report for definition.

incontinence supplies and glasses for Medicaid recipients, miscellaneous contracts of DCH's hospitals and centers, and contracts awarded by the Michigan Department of Information Technology\*. Accordingly, we do not express any conclusions related to these grant agreements and contracts.

### Audit Methodology

We conducted a preliminary review of DCH's contracting and granting processes to gain an understanding of the contracting and granting activities within DCH to form a basis for defining our audit scope. Our preliminary review included interviewing various DCH contracting and program staff; reviewing applicable laws, rules, regulations, policies, procedures, manuals, and guidelines; examining reports from various internal and external audits and reviews; obtaining an understanding of DCH's internal control\*; reviewing records for selected contracts and grant agreements; and analyzing available contract and grant agreement information recorded in DCH's Contract Tracking System.

To accomplish our objectives, we selected a risk-based judgmental sample of 15 contracts and grant agreements to review. We developed and used standard interview forms and file review work sheets to complete and document our audit activities.

To accomplish our first objective, we interviewed DCH contracting and granting staff to obtain information regarding the processes and procedures used in the development of the contracts and grant agreements. Also, we reviewed 15 contract and grant agreement files for evidence of clear and appropriate work statements, detailed budgets, measurable performance standards\* with defined output\* and/or outcome\* levels, and reasonable evaluation methods. In addition, we examined DCH's use of performance incentives, contract and grant agreement administrator\* involvement in the development of the contracts and grant agreements, the timeliness of the execution of the contracts and grant agreements, and changes to executed contracts and grant agreements.

To accomplish our second objective, we interviewed DCH contracting and granting staff to obtain information regarding the processes and procedures used in selecting contractors and grantees. Also, we reviewed 15 contracts and grant agreements and their supporting documentation to determine if DCH considered contractors' and grantees' prior experience during the selection process; if contract and grant agreement

\* See glossary at end of report for definition.

administrators disclosed conflicts of interest; and if DCH used competitive selection procedures or allocated grant funds according to established methodologies.

To accomplish our third objective, we interviewed DCH contracting and granting staff to obtain information regarding the processes and procedures used to monitor and evaluate contractor and grantee performance. Also, we reviewed 15 contract and grant agreement files to assess the appropriateness of DCH's monitoring and evaluation activities, including verifying reported performance and financial data against supporting documentation. In addition, we assessed whether DCH contract and grant administrators appropriately authorized contractors' and grantees' requests for payment. Further, we determined whether DCH ensured that contract and grant administrators were appropriately trained.

When selecting activities or programs for audit, we use an approach based on assessment of risk and opportunity for improvement. Accordingly, we focus our audit efforts on activities or programs having the greatest probability for needing improvement as identified through a preliminary review. Our limited audit resources are used, by design, to identify where and how improvements can be made. Consequently, we prepare our performance audit reports on an exception basis.

#### Agency Responses

Our audit report contains 5 findings and 5 corresponding recommendations. DCH's preliminary response indicated that it agrees with all 5 recommendations.

The agency preliminary response that follows each recommendation in our report was taken from the agency's written comments and oral discussion subsequent to our audit fieldwork. Section 18.1462 of the *Michigan Compiled Laws* and the State of Michigan Financial Management Guide (Part VII, Chapter 4, Section 100) require DCH to develop a formal response to our audit findings and recommendations within 60 days after release of the audit report.

COMMENTS, FINDINGS, RECOMMENDATIONS,  
AND AGENCY PRELIMINARY RESPONSES

# EFFECTIVENESS IN DEVELOPING SERVICE-RELATED CONTRACTS AND GRANT AGREEMENTS

## COMMENT

**Audit Objective:** To assess the effectiveness of the Department of Community Health's (DCH's) efforts to ensure that selected service-related contracts and grant agreements contained comprehensive service descriptions, detailed budgets, performance criteria, and monitoring provisions.

**Audit Conclusion:** We concluded that DCH's efforts to ensure that selected service-related contracts and grant agreements contained comprehensive service descriptions, detailed budgets, performance criteria, and monitoring provisions were moderately effective. Our assessment disclosed two reportable conditions\* related to contract and grant agreement development and contract and grant agreement administrator training (Findings 1 and 2).

## FINDING

### 1. Contract and Grant Agreement Development

DCH needs to improve its controls for ensuring the sufficient development and timely completion of detailed performance-based service contracts and grant agreements. Without sufficiently developed performance-based service contracts and grant agreements, DCH could not ensure that purchased services were fully delivered in a timely manner.

We reviewed 15 contracts and grant agreements totaling \$87.4 million and noted:

- a. DCH did not sufficiently identify the required deliverables, the associated time frames for delivery, or the criteria for evaluating the contractor's or grantee's performance in 6 (40.0%) contracts and grant agreements totaling \$20.9 million. For example, the entire service description for a \$1.6 million component of a \$5.6 million grant agreement required the grantee to act as an eligibility clearinghouse for the State's Medicaid program. The grant agreement stated that this included developing, supporting, and maintaining systems for real-time and batch inquiries on eligibility. Several systems were

\* See glossary at end of report for definition.

identified as needing support; however, the systems requiring development were not identified. To enable it to effectively monitor the grant, DCH should have identified the specific systems requiring development, the required time frame(s) for development, and the technical specifications. Also, the budget for the grant agreement included \$1.0 million for transaction fees to be paid to a named subcontractor. However, the grant agreement did not identify the nature or type of transactions to be processed or the cost associated with processing each transaction. In addition, the budget included approximately \$65,000 for equipment; however, there was no identification of the items to be purchased.

A detailed description of work that clearly identifies the required deliverables would establish DCH's expectations for the contractor or grantee and, correspondingly, provide the basis for monitoring and evaluating the contractor's or grantee's performance.

Generally, each DCH program area was responsible for developing the work statement and evaluation criteria for its own contracts and/or grant agreements. Although DCH's Contract Management Section (CMS) offered the program areas assistance in the contract and grant agreement development process, if requested, CMS did not have responsibility for ensuring the propriety of the work statements or evaluation criteria included therein.

- b. DCH did not formalize significant changes to 3 (20.0%) contracts and grant agreements by processing written amendments to them. The 3 contracts totaled \$53.8 million. In one example, both the type and quantity of services that DCH expected the grantee to deliver changed significantly (both increases and decreases). Failure to properly control changes could result in unintentional modifications to the scope of work, circumvention of internal control, and reduced grantee accountability.

Failure to process the written amendments may have been caused by control deficiencies that did not adequately identify the types of changes that required the processing of written amendments.

- c. DCH did not sign 1 (6.7%) grant agreement totaling approximately \$4.0 million until one week after the effective date of the grant agreement. To properly

protect the interest of the State, DCH should ensure that both it and the applicable grantees sign grant agreements prior to the effective date of the respective grant agreements.

- d. DCH did not utilize accountability provisions, other than the provision to withhold payment for late reporting, in its contracts or grant agreements. Properly developed accountability provisions (both financial and nonfinancial) that reinforce positive performance or penalties for failing to meet minimum performance standards are recognized as a best practice by organizations such as the United States Government Accountability Office and others for improving contractor/grantee performance.

### **RECOMMENDATION**

We recommend that DCH improve its controls for ensuring the sufficient development and timely completion of detailed performance-based service contracts and grant agreements.

### **AGENCY PRELIMINARY RESPONSE**

DCH agrees with the recommendation to improve its controls for ensuring the sufficient development and timely completion of detailed performance-based service contracts and grant agreements. For grant agreements beginning October 1, 2010, DCH will require the use of its detailed statement of work for all grant agreements and will reiterate its requirement that all grant agreements be signed prior to their applicable start dates. The grant agreement instructions will emphasize that significant changes in scope of work, time lines, and deliverables in addition to changes in funding and agreement period must be reflected in an amendment. As DCH migrates to an electronic grants management system over the next two years, detailed performance objectives and outcomes will be required. For contracts, the Grants and Purchasing Division will continue to utilize the required Department of Technology, Management & Budget (DTMB) contract templates and will provide guidelines to contract managers on the contract change notice criteria and process to ensure that all necessary contract changes are captured in a contract amendment. DCH stated that, where feasible, it does incorporate penalties for failing to meet the minimum performance standards.

## **FINDING**

### **2. Contract and Grant Agreement Administrator Training**

DCH did not establish training requirements for or ensure that it provided training to its contract and grant agreement administrators. As a result, DCH could not ensure that its contract and grant agreement administrators had the necessary knowledge and skills to satisfactorily perform their contracting and granting-related responsibilities.

Section 2-18.1 of the *Michigan Civil Service Commission Rules* assigns the primary responsibility for staff training to agency management. CMS provides contract and grant-related training to DCH employees upon request. However, contrary to best practices identified by the Office of Federal Procurement Policy and others, DCH has not established mandatory training requirements for its contract and grant agreement administrators.

Contract and grant agreement administrators are responsible for the development of work statements, service delivery schedules, performance and reporting requirements, and other items incorporated into DCH's contracts and grant agreements. As important, the contract and grant agreement administrators are also responsible for the development, execution, and documentation of cost-effective contract and grant agreement monitoring and evaluation activities. Together, execution of these responsibilities should help to ensure that DCH is getting the quality and quantity of services that it is paying for. The large dollar amount and complexity of many of DCH's contracts and grant agreements magnifies the critical nature of these responsibilities.

We interviewed the administrators of 15 contracts and grant agreements totaling \$87.4 million. In 5 (33.3%) instances, the contract and grant agreement administrators expressed a need for some form of contract or grant agreement administration training. In addition, our findings related to contract and grant agreement development, monitoring and evaluation, and conflict of interest demonstrate additional training needs. Adequate training is essential to ensure that contract and grant agreement administrators possess the knowledge and skills required to effectively complete their responsibilities.

## **RECOMMENDATION**

We recommend that DCH establish training requirements for and ensure that it provides training to its contract and grant agreement administrators.

## **AGENCY PRELIMINARY RESPONSE**

DCH agrees with the recommendation to establish training requirements for and ensure that it provides training opportunities to its contract and grant agreement administrators. DCH stated that subsequent to the audit period, its Grants and Purchasing Division teamed with the Department of Management and Budget's (DMB's) Purchasing Operations to sponsor contract management, contract administration, and work statement development training sessions for all contract and grant agreement administrators within DCH. DCH also stated that these trainings continue to be available on a periodic basis for new contract and grant agreement administrators. In addition, DCH stated that additional contract and grant agreement administrator training is available and provided by the federal grant programs for the federal grant awards received by DCH. The Grants and Purchasing Division will establish a training curriculum and monitoring system for DCH's contract and grant agreement administrators. However, DCH stated that because of staffing limitations and significant daily work loads, the Grants and Purchasing Division will not be able to directly provide most of the training. The manager overseeing each contract and grant agreement administrator will be responsible for ensuring that the contract and grant agreement administrator is complying with monitoring and evaluation requirements for the contracts and/or grant agreements that he or she administers.

## **EFFECTIVENESS IN AWARDING SERVICE-RELATED CONTRACTS AND GRANT AGREEMENTS**

### **COMMENT**

**Audit Objective:** To assess the effectiveness of DCH's efforts to ensure that it awarded selected service-related contracts and grant agreements on a fair and competitive basis.

**Audit Conclusion:** We concluded that DCH's efforts to ensure that it awarded selected service-related contracts and grant agreements on a fair and competitive basis were moderately effective. Our assessment disclosed two reportable

conditions related to contract and grant awarding processes and conflict of interest disclosure (Findings 3 and 4).

## **FINDING**

### **3. Contract and Grant Awarding Processes**

DCH needs to improve its controls over its contract and grant awarding processes. As a result of its control weaknesses, DCH could not demonstrate that it awarded some contracts and grants fairly and that it obtained the best value for the State.

We reviewed DCH's contractor and grantee selection and grant funding processes for 15 contracts and grant agreements totaling \$87.4 million and noted:

- a. DCH awarded 2 (13.3%) grants (1 noncompetitively and 1 competitively) totaling \$12.4 million to acquire information technology-related services that were not within its delegated purchasing authority. DMB delegated to DCH the authority to enter into grant agreements in any amount. However, these services did not meet the State's commodity code definition for a grant or DCH's criteria for a grant (versus a contract) and greatly exceeded DCH's delegated purchasing authority. Consequently, DCH should have forwarded requests to purchase these services to DMB or the Michigan Department of Information Technology (MDIT), as appropriate, at the time of the grant award.

For example, DCH awarded the noncompetitive grant in 2001 for \$1.2 million and subsequently amended it 11 times. These amendments expanded the scope of the original grant agreement to include various new systems and applications, increased the grant award by \$6.8 million, and extended the term of the grant from September 30, 2002 to December 31, 2008. Given the large scope and substantial costs of the services included in the grant agreement, the contracting process should have been completed by DMB using one or more competitive solicitations. DCH's delegated purchasing authority of \$250,000 in 2001 was reduced to \$25,000 effective March 25, 2003.

Without a fair and open competitive bidding process, DCH could not be assured that it obtained the desired services at the best price. Also, failure to follow established purchasing procedures could result in DCH losing its delegated purchasing authority.

- b. DCH did not adequately document that it awarded 2 (13.3%) grants totaling \$1.8 million in accordance with its identified funding methodologies. Also, DCH did not adequately identify its funding methodology for 1 (6.7%) grant totaling \$741,000. All three of these grants were part of larger grant programs that each used a single methodology to make numerous awards annually.

The establishment and documented use of a clear and consistent funding methodology are needed to ensure and demonstrate that DCH awarded grants in a fair and equitable manner and in conjunction with each applicable program's stated priorities.

- c. DCH did not consider or document that it considered 5 grantees' prior performance before entering into new grant agreements with them totaling \$8.9 million.

Although we did not identify any poor performance on the part of the 5 grantees, sound business practice dictates that DCH consider, and document its consideration of, grantees' prior performance before entering into new grant agreements with them.

## **RECOMMENDATION**

We recommend that DCH improve its controls over its contract and grant awarding processes.

## **AGENCY PRELIMINARY RESPONSE**

DCH agrees with the recommendation to improve controls over its contract and grant awarding processes. DCH stated that the director of the DMB Office of Purchasing delegated authority to DCH to competitively bid the information technology-related services referenced in part a. of the finding. DCH also stated that MDIT concurred with DCH in making this purchase; however, MDIT's concurrence was not documented. DCH informed us that it was granted authority to make the purchase because the services were related to a boilerplate provision requiring the demonstration project and because the services were linked to DCH's Medicaid Management Information System. DCH stated that the original grant agreement for the noncompetitively bid grant referenced in part a. was bid by DCH's Office of Services to the Aging (OSA). DCH also stated that as the services required by OSA and the federal government changed, OSA decided to reduce the

scope of the original contract and work only with the prime subcontractor who was providing the specific portion of services that OSA needed going forward. DCH informed us that, as an interim measure to maintain access to critical data needed for federal reporting, DCH (with the verbal approval of MDIT) contracted with the prime subcontractor until MDIT was able to competitively rebid the services. However, DCH stated that it was several years before MDIT was in a position to competitively rebid the information technology services. DCH informed us that the services were rebid in fiscal year 2008-09 and a new grant agreement has been in place since November 2009.

DCH will continue to evaluate purchase requests to ensure that the appropriate purchasing requirements and processes are adhered to in accordance with State and federal requirements. Further, DCH will issue guidelines to grant agreement administrators to use consistent funding methodologies and criteria that will ensure fair and equitable grant awards based on each program's stated priorities. DCH stated that because of the timing of grant development and the award and execution of grant agreements, one complete fiscal year cycle may not be completed before it is time to issue a subsequent year grant award. Consequently, DCH will issue guidelines to grant agreement administrators for documenting a grantee's performance prior to issuing the subsequent year's grant agreement.

## **FINDING**

### **4. Conflict of Interest Disclosure**

DCH did not have effective controls for ensuring that employees involved in the selection, monitoring, and evaluation of contractors and grantees were free of conflicts of interest. As a result, DCH could not ensure that it timely identified and took appropriate measures to avoid conflicts of interest by employees involved in the selection, monitoring, and evaluation of contractors and grantees.

Section 2-8.3 of the *Michigan Civil Service Commission Rules* requires each State employee to annually report all personal or financial interests that the employee or members of the employee's immediate family may have in any business or entity that the employee will have direct contact with in performing the employee's official State duties.

In our review of 15 contracts and grant agreements, we identified one or more individuals involved in the selection, monitoring, and/or evaluation of 9 (60.0%) of the contracts and grant agreements who had not completed or timely completed or could not document that they completed an annual conflict of interest disclosure form. Moreover, DCH employees working with 3 of the 9 contracts and grants informed us that they were not aware of the annual disclosure requirement.

On March 27, 2006, DCH's director issued an administrative directive to all DCH employees reminding them of the need to complete the annual disclosure required by the aforementioned Civil Service Commission rule. The administrative directive required employees to complete the attached disclosure form and return it to DCH's Human Resources Division. Notwithstanding, DCH did not establish controls to ensure that DCH employees completed and returned the disclosure forms to the Human Resources Division following issuance of the administrative directive or annually thereafter.

### **RECOMMENDATION**

We recommend that DCH establish effective controls for ensuring that employees involved in the selection, monitoring, and evaluation of contractors and grantees are free of conflicts of interest.

### **AGENCY PRELIMINARY RESPONSE**

DCH agrees with the recommendation to establish effective controls for ensuring that employees involved in the selection, monitoring, and evaluation of contractors and grantees are free of conflicts of interest. DCH stated that although its Human Resources Office obtained annual disclosure forms and updates for some DCH employees during the audit period, it did not verify that all employees responded to the annual disclosure request. As a result, in September 2010 the Human Resources Office plans to issue a new request for annual disclosure forms in compliance with Michigan Civil Service Commission Rules and will verify that it receives a disclosure form from each employee. DCH stated that as new employees are hired, they are required to sign a disclosure form for placement in their personnel files. In addition, each September, the Human Resources Office will request annual disclosure form updates from employees and will verify that all new employees hired during the previous fiscal year have a completed disclosure form in their personnel files.

## **EFFECTIVENESS IN MONITORING AND EVALUATING CONTRACTORS AND GRANTEES**

### **COMMENT**

#### **Audit Objective:**

To assess the effectiveness of DCH's efforts to monitor and evaluate the performance of selected contractors and grantees.

**Audit Conclusion: We concluded that DCH's efforts to monitor and evaluate the performance of selected contractors and grantees were moderately effective.** Our assessment disclosed one reportable condition related to contract and grant agreement monitoring and evaluation (Finding 5).

### **FINDING**

#### **5. Contract and Grant Agreement Monitoring and Evaluation**

DCH did not establish sufficient controls to ensure that its contract and grant agreement administrators sufficiently monitored and evaluated DCH's contracts and grant agreements. As a result, DCH could not ensure or could not document that it ensured that contractors and grantees complied with the terms of their DCH contracts and grant agreements.

DMB Administrative Guide policy 0610 requires DCH to manage its contracts in a fiscally responsible manner and ensure that contractors fully comply with their contractual responsibilities. Also, the Office of Federal Procurement Policy and others have identified various best practices for monitoring and evaluating contractor performance. Use of these practices should help DCH to ensure that its contractors and grantees fulfill the responsibilities of their contracts and grant agreements.

We reviewed 15 contracts and grant agreements totaling \$87.4 million and noted:

- a. DCH contract and grant agreement administrators did not sufficiently monitor the financial provisions of 8 (53.3%) contracts and grant agreements totaling \$17.3 million. Specifically:
  - (1) DCH grant agreement administrators did not obtain, review for propriety, and authorize grantees' requests for payments for 2 grant agreements totaling \$9.6 million.
  - (2) DCH contract and grant agreement administrators did not sufficiently review the documentation supporting contractors' and grantees' requests for payments for 6 contracts and grant agreements totaling \$7.7 million.

The payment terms associated with all 8 contracts and grant agreements required DCH to reimburse the contractors and grantees for their actual costs to provide the required services. As such, DCH contract and grant agreement administrators should have ensured that the reported costs were appropriate for each respective contract or grant agreement. For example, a \$5.6 million grant agreement included approximately \$1.3 million for the salaries and wages of a defined number of full-time equivalent positions (e.g., project managers, programmers, and business analysts) and \$3.2 million for various subcontracted services. DCH should have identified the key components of these contracts and grant agreements and established processes to monitor and evaluate them.

Contract or grant agreement administrator's review and authorization for payment of contractor/grantee billings are recognized as a best practice by the National State Auditors Association and the Office of Federal Procurement Policy.

- b. DCH grant agreement administrators did not sufficiently monitor or monitor and evaluate 6 (40.0%) grant agreements totaling \$10.5 million. For example, DCH could not provide documentation that the grant agreement administrator for the \$5.6 million grant agreement mentioned in part a. of this finding had acknowledged the receipt of the required deliverables. As a second example, a grantee was required to create an assessment tool to evaluate and demonstrate the effectiveness of some of its grant-related services. However,

the grantee did not provide evidence to the grant agreement administrator that it had created and used the required assessment tool.

Effective monitoring and evaluation by contract and grant agreement administrators should increase the probability that services are successfully completed in a timely manner. Also, effective monitoring should uncover difficulties that, if unnoticed, could lead to poor or untimely provision of services.

### **RECOMMENDATION**

We recommend that DCH establish sufficient controls to ensure that its contract and grant agreement administrators sufficiently monitor and evaluate DCH's contracts and grant agreements.

### **AGENCY PRELIMINARY RESPONSE**

DCH agrees with the recommendation to establish sufficient controls to ensure that its contract and grant agreement administrators sufficiently monitor and evaluate DCH's contracts and grant agreements. DCH stated that in prior audits, it was cited for not processing contract and grant agreement payments timely and, as a result, revised its process to require the direct submission of all contract and grant agreement payment requests to the DCH Accounting Division for processing. Also, DCH stated that if there were any programmatic deficiencies or failed performance or some other exception by the contractor or grantee that would require an adjustment in their payment, it was the responsibility of the contract or grant agreement administrator to advise the DCH Accounting Division of the need for an adjustment in a subsequent period. DCH informed us that its current standard practice for contract and grant agreement payments provides for a post review of the contract and grant payment requests by the contract or grant agreement administrators and subsequent period adjustments. DCH stated that through recent subrecipient monitoring efforts, DCH has begun performing more thorough reviews of contractors and grantees and their subcontractors and subgrantees using subrecipient monitoring tools that were developed by DCH's audit staff in conjunction with the federal requirements on subrecipient monitoring. DCH will issue guidelines to its contract and grant agreement administrators on monitoring and evaluation expectations and documentation, including both program and financial reporting documentation and deliverables. With the implementation of the electronic grants management system, all payment requests will be first approved by the grant

agreement administrator and second by the DCH Accounting Division before the payment requests may be released through an interface to MAIN for payment. All program, financial, and statistical reports and program deliverables will be captured electronically and attached/linked to the grant agreement record for ease of program monitoring and evaluation.

# GLOSSARY

## Glossary of Acronyms and Terms

administrator	The individual assigned the responsibility to manage the contract or grant agreement.
CMS	Contract Management Section.
contract	A legally binding agreement between the State and a vendor to purchase specific goods or services at an agreed-upon price.
DCH	Department of Community Health.
Department of Management and Budget (DMB)	Executive Order No. 2009-55 renamed the Department of Management and Budget as the Department of Technology, Management & Budget (DTMB), effective March 21, 2010. It also transferred all of the authority, powers, duties, functions, responsibilities, records, personnel, property, equipment, and appropriations of the Michigan Department of Information Technology (MDIT) to DTMB by a Type III transfer and abolished MDIT.
DTMB	Department of Technology, Management & Budget.
effectiveness	Program success in achieving mission and goals.
grant agreement	A type of contract that typically awards money to local units of government and nonprofit entities for goods or services that directly benefit the recipient of the grant.
internal control	The plan, policies, methods, and procedures adopted by management to meet its mission, goals, and objectives. Internal control includes the processes for planning, organizing, directing, and controlling program operations. It includes the systems for measuring, reporting, and monitoring program performance. Internal control serves as

a defense in safeguarding assets and in preventing and detecting errors; fraud; violations of laws, regulations, and provisions of contracts and grant agreements; or abuse.

Michigan Department  
of Information  
Technology (MDIT)

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monitoring

Ongoing reviews of the contractor's or grantee's activities to ensure that the responsibilities of the contract are being performed satisfactorily, including the approval of billings.

OSA

Office of Services to the Aging.

outcome

An actual impact of a program or an agency.

output

A product or a service produced by a program or an agency.

performance audit

An economy and efficiency audit or a program audit that is designed to provide an independent assessment of the performance of a governmental entity, program, activity, or function to improve program operations, to facilitate decision making by parties responsible for overseeing or initiating corrective action, and to improve public accountability.

performance standard

A desired level of output or outcome.

reportable condition

A matter that, in the auditor's judgment, falls within any of the following categories: an opportunity for improvement within the context of the audit objectives; a deficiency in internal control that is significant within the context of the objectives

of the audit; all instances of fraud; illegal acts unless they are inconsequential within the context of the audit objectives; significant violations of provisions of contracts or grant agreements; and significant abuse that has occurred or is likely to have occurred.





