PERFORMANCE AUDIT
OF THE

CLOSURE OF JOSEPH M. SNYDER MACOMB-OAKLAND REGIONAL CENTER

DEPARTMENT OF COMMUNITY HEALTH

August 1999

39-330-98

EXECUTIVE DIGEST

CLOSURE OF JOSEPH M. SNYDER MACOMB-OAKLAND REGIONAL CENTER

INTRODUCTION	This report, issued in August 1999, contains the results of our performance audit* of the Closure of Joseph M. Snyder Macomb-Oakland Regional Center (MORC), Department of Community Health (DCH).
AUDIT PURPOSE	This performance audit was conducted as part of the constitutional responsibility of the Office of the Auditor General. Performance audits are conducted on a priority basis related to the potential for improving effectiveness* and efficiency* .
BACKGROUND	MORC, located in Clinton Township, Michigan, was an agency of DCH. In July 1995, DCH initiated a process to transfer the systems of programs and services operated through MORC to a nonprofit entity called Macomb-Oakland Regional Center, Inc. (MORC, Inc.). On September 27, 1996, MORC ceased existence as a State agency. Effective September 28, 1996, MORC, Inc., began to deliver, either directly or through contract, the services previously delivered by MORC. MORC, Inc., operates its programs under contract with several county community mental health services programs.

* *See glossary at end of report for definition.*

MORC provided direct clinical support and housing development services* for both developmentally disabled* and mentally ill* recipients* and subcontracted for residential services*. Clinical support services included support coordination; nursing; psychology; occupational, speech, and recreation therapy; dietary; medical; psychiatry; and employment services.

As of September 27, 1996, MORC was serving approximately 1,600 developmentally disabled and 400 mentally ill recipients. MORC's fiscal year 1995-96 expenditures totaled approximately $120 million.

AUDIT OBJECTIVES, CONCLUSIONS, AND NOTEWORTHY ACCOMPLISHMENT

Audit Objective: To determine if DCH resolved appeals to and collected amounts due from its cost settlements* with MORC's residential services providers.

Conclusion: We determined that DCH did not resolve some appeals to, and did not collect amounts due from, its cost settlements with MORC's residential services providers. Our audit disclosed one material condition*:

- DCH, in conjunction with MORC, did not attempt to collect final cost settlement amounts due to the State from MORC's residential services providers (Finding 1).

  DCH agrees with the finding and recommendation.

Our audit also disclosed a reportable condition* related to cost settlement appeals (Finding 2).

Audit Objective: To determine if DCH had adequate controls over MORC's real* and personal property*.

* *See glossary at end of report for definition.*

Conclusion: We determined that DCH had adequate controls over MORC's real property but did not have adequate controls over MORC's personal property. Our audit disclosed one reportable condition related to controls over personal property (Finding 3).

Audit Objective: To determine if the termination settlements for MORC's employees were accurate.

Conclusion: We determined that the termination settlements for MORC's employees were generally accurate. However, our audit disclosed one reportable condition related to sick and annual leave payoffs (Finding 4).

Audit Objective: To determine if DCH complied with selected laws, rules, and regulations in the closure of MORC.

Conclusion: We determined that DCH generally complied with selected laws, rules, and regulations in the closure of MORC. However, our audit disclosed one reportable condition related to conflict of interest* (Finding 5).

Audit Objective: To determine if DCH ensured that the rights of MORC's recipients were protected subsequent to the closure of MORC.

Conclusion: We determined that DCH ensured that the rights of MORC's recipients were protected subsequent to the closure of MORC.

* *See glossary at end of report for definition.*

Noteworthy Accomplishment: DCH, in conjunction with the Detroit-Wayne, Oakland, and Macomb county community mental health services programs, and MORC, Inc., directed the transition of MORC's service delivery system from MORC to MORC, Inc., in approximately 12 months. Throughout the transition, DCH ensured active family and recipient involvement in service planning, stability in the areas of housing, community, relationships, support systems, and funding. As a result, DCH accomplished the transition with little or no disruption in services to the recipients. The transition required, among other things, the assurance of a stable work force of over 350 employees, the transfer of responsibility for over 2,000 recipients, and the conversion of all functions associated with operating MORC. Some of these functions, including (but not limited to) accounting, financial reporting, and payroll and personnel, required extensive development because the State had provided the functions prior to the transition.

AUDIT SCOPE AND METHODOLOGY

Our audit scope was to examine the program and other records of the Joseph M. Snyder Macomb-Oakland Regional Center. Our audit was conducted in accordance with *Government Auditing Standards* issued by the Comptroller General of the United States and, accordingly, included such tests of the records and such other auditing procedures as we considered necessary in the circumstances.

We examined MORC's records and activities for the period July 1995 through February 1999. To accomplish our objectives, we reviewed DCH, DMB, and the Department of Civil Service (DCS) policies and procedures, along with applicable laws, rules, and regulations. We interviewed DCH, DMB, DCS, and MORC, Inc., staff.

We examined selected cost settlements in the appeals process and evaluated DCH's efforts to resolve the appeals. We also examined selected final cost settlements and evaluated DCH's efforts to collect amounts due to the State.

We evaluated the appropriateness of DCH's efforts to account for equipment and furnishings being used by MORC, Inc. We conducted a limited physical inventory of State-owned equipment and furnishings used by MORC, Inc. We determined whether DCH executed leases with MORC, Inc., for its use of State-owned real property.

We evaluated the adequacy of DCH's internal control structure* over termination settlements. We also assessed the accuracy of selected employee termination settlements.

We interviewed community mental health services program staff and MORC, Inc., advocacy organizations. We assessed whether there were sufficient recipient rights staff to process recipient rights complaints in a timely manner. We evaluated whether recipient rights staff were adequately trained prior to assuming their duties. We examined selected recipient rights complaints to assess whether they were investigated and resolved in a timely and appropriate manner.

We evaluated DCH's compliance with boilerplate provisions of Act 151, P.A. 1995, and Act 352, P.A. 1996. We assessed whether participants in the closure process were free of conflicts of interest. We reviewed the legality of providing start-up funding to MORC, Inc., and of MORC,

* *See glossary at end of report for definition.*

Inc., using the name of the State agency without making payment to the State. We also determined whether DCH had any responsibility for ensuring that MORC employees who elected to work for MORC, Inc., received employment benefits similar to those that they received from the State.

AGENCY RESPONSES AND CLOSING REVIEW FOLLOW-UP

Our audit report includes 5 findings and 8 corresponding recommendations. DCH concurred with all of the findings and informed us that it has taken action or will take action to implement the recommendations.

DCH complied with 1 of the recommendations from our March 1997 closing review* of MORC that were included within the scope of this audit. We are repeating 1 recommendation in this report.

* *See glossary at end of report for definition.*

Mr. James K. Haveman, Jr., Director
Department of Community Health
Lewis Cass Building
Lansing, Michigan

Dear Mr. Haveman:

This is our report on the performance audit of the Closure of Joseph M. Snyder Macomb-Oakland Regional Center, Department of Community Health.

This report contains our executive digest; description of agency; audit objectives, scope, and methodology and agency responses and closing review follow-up; 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.

Sincerely,

Thomas H. McTavish, C.P.A.
Auditor General

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Description of Agency

The Joseph M. Snyder Macomb-Oakland Regional Center (MORC), located in Clinton Township, Michigan, was an agency of the Department of Community Health (DCH). In July 1995, DCH initiated a process to transfer the systems of programs and services operated through MORC to a nonprofit entity called Macomb-Oakland Regional Center, Inc. (MORC, Inc). On September 27, 1996, MORC ceased existence as a State agency. Effective September 28, 1996, MORC, Inc., began to deliver, either directly or through contract, the services previously delivered by MORC. MORC, Inc., operates its programs under contract with several county community mental health services programs.

MORC provided direct clinical support and housing development services for both developmentally disabled and mentally ill recipients and subcontracted for residential services. Clinical support services included support coordination; nursing; psychology; occupational, speech, and recreation therapy; dietary; medical; psychiatry; and employment services.

MORC's operations were directed by eight commitments. For example, MORC committed to help its recipients become a part of the community by promoting the concepts of acceptance, dignity, and respect and by providing opportunities for new experiences for each person. MORC also committed to assisting recipients to increase their sense of responsibility, contribute to the community, enjoy life, and to help recipients find a sense of belonging and a place in the world that is safe, secure, and comfortable.

As of September 27, 1996, MORC was serving approximately 1,600 developmentally disabled and 400 mentally ill recipients. MORC's fiscal year 1995-96 expenditures totaled approximately $120 million.

Audit Objectives, Scope, and Methodology and Agency Responses and Closing Review Follow-Up

Audit Objectives

Our performance audit of the Closure of Joseph M. Snyder Macomb-Oakland Regional Center (MORC) had the following objectives:

1. To determine if the Department of Community Health (DCH) resolved appeals to and collected amounts due from its cost settlements with MORC's residential services providers.

2. To determine if DCH had adequate controls over MORC's real and personal property.

3. To determine if the termination settlements for MORC's employees were accurate.

4. To determine if DCH complied with selected laws, rules, and regulations in the closure of MORC.

5. To determine if DCH ensured that the rights of MORC's recipients were protected subsequent to the closure of MORC.

Audit Scope

Our audit scope was to examine the program and other records of the Joseph M. Snyder Macomb-Oakland Regional Center. Our audit was conducted in accordance with *Government Auditing Standards* issued by the Comptroller General of the United States and, accordingly, included such tests of the records and such other auditing procedures as we considered necessary in the circumstances.

Audit Methodology

Our audit procedures were performed during the months of September 1998 through February 1999 and included examining DCH's records and activities for the period February 1995 through February 1999.

To accomplish our first objective, we reviewed DCH policies and procedures related to cost settlement and cost settlement appeals. We also reviewed the Department of Management and Budget (DMB) procedures for collection of amounts due to the State. We interviewed DCH staff responsible for completing cost settlements, processing appeals, and collecting amounts due to the State. We examined selected cost settlements in the appeals process and evaluated DCH's efforts to resolve the appeals. We also examined selected final cost settlements and evaluated DCH's efforts to collect amounts due to the State.

To accomplish our second objective, we reviewed DCH and DMB policies and procedures related to real and personal property and interviewed DCH, DMB, and MORC, Inc., staff. We evaluated the appropriateness of DCH's efforts to account for State-owned equipment and furnishings used by MORC, Inc. We assessed whether DCH complied with DMB procedures when it disposed of some personal property that had been in use by MORC, Inc. We conducted a limited physical inventory of State-owned equipment and furnishings in use by MORC, Inc. We determined whether DCH executed leases with MORC, Inc., for its use of State-owned real property.

To accomplish our third objective, we reviewed applicable Department of Civil Service (DCS) rules and retirement statutes and interviewed DCS, DCH, and MORC, Inc., staff. We documented and evaluated the adequacy of DCH's internal control structure over termination settlements. We also assessed the accuracy of selected employee termination settlements.

To accomplish our fourth objective, we reviewed applicable sections of the Mental Health Code along with community mental health services program policies and procedures related to recipient rights. We interviewed DCH and community mental health services program staff, along with MORC, Inc., advocacy organizations. We assessed whether there were sufficient recipient rights staff to process recipient rights complaints in a timely manner. We evaluated whether recipient rights staff were adequately trained prior to assuming their duties. We examined selected recipient rights complaints to assess whether they were investigated and resolved in a timely and appropriate manner.

To accomplish our fifth objective, we reviewed applicable DCH and DCS policies and procedures and interviewed DCH and DCS staff along with MORC, Inc., advocacy

organizations. We evaluated DCH's compliance with boilerplate provisions of Act 151, P.A. 1995, and Act 352, P.A. 1996. We assessed whether participants in the closure process were free of conflicts of interest. We reviewed the legality of providing start-up funding to MORC, Inc., and of MORC, Inc., using the name of the State agency without making payment to the State. We also determined whether DCH had any responsibility for ensuring that MORC employees who elected to work for MORC, Inc., received employment benefits similar to those that they received from the State.

Agency Responses and Closing Review Follow-Up

Our audit report contains 5 findings and 8 corresponding recommendations. DCH concurred with all of the findings and informed us that it has taken action or will take action to implement the recommendations.

DCH complied with 1 of the recommendations from our March 1997 closing review of MORC that were included within the scope of this audit. We are repeating 1 recommendation in this report.

COMMENTS, FINDINGS, RECOMMENDATIONS, AND AGENCY PRELIMINARY RESPONSES

COST SETTLEMENT

COMMENT

Audit Objective: To determine if the Department of Community Health (DCH) resolved appeals to and collected amounts due from its cost settlements with Joseph M. Snyder Macomb-Oakland Regional Center's (MORC's) residential services providers.

Conclusion: We determined that DCH did not resolve some appeals to, and did not collect amounts due from, its cost settlements with MORC's residential services providers. We consider this to be a material condition. Our audit also disclosed a reportable condition related to cost settlement appeals.

FINDING

1. Cost Settlement Collections

DCH, in conjunction with MORC, did not attempt to collect final cost settlement amounts due to the State from MORC's residential services providers.

MORC entered into net cost contracts with its residential services providers for fiscal year 1992-93 and fiscal year 1993-94 (ended March 31, 1994). Net cost contracts required cost settlement at fiscal year-end. Cost settlement, the final reconciliation and adjustment of contractor revenues and expenditures, often resulted in contractors owing the State for amounts that MORC had overfunded them.

In compliance with DCH Administrative Directive 01-c-1116(j)-AD-17, DCH directed overfunded residential services providers to repay MORC within 30 days of notification of cost settlement. In cases of financial hardship, the directive permitted repayment over a period not to exceed one year. DCH Guideline 08-C-1838/GL required MORC to make every effort to collect these debts. Subsequent to MORC's closure, DCH was responsible for making collection.

As of December 1, 1998, DCH records indicated that 78 residential services providers owed DCH approximately $1.9 million for final cost settlements from

fiscal year 1992-93 and fiscal year 1993-94 (ended March 31, 1994). We analyzed DCH and MORC records for 23 cost settlements totaling $456,029. We noted that DCH approved a payment plan for one provider, but DCH did not make any related collections. We noted no collection efforts for any of the 23 cost settlements. Also, DCH did not direct the residential services providers to remit payment to DCH after MORC's closure on September 27, 1996.

DCH's delay at pursuing collection of amounts due to the State by MORC's residential services providers was a result, in part, of the time DCH took to decide on a collection methodology. The collection methodology was at issue because DCH was uncertain if it or MORC made any prior collections on the outstanding accounts.

DCH would have increased the likelihood of collecting amounts due to the State if it had conducted collection efforts in a timely manner. DCH's continued delays further reduce DCH's opportunity for collection.

RECOMMENDATION

We recommend that DCH attempt to collect amounts due to the State from the cost settlement with MORC's residential services providers.

AGENCY PRELIMINARY RESPONSE

DCH agrees with the finding and recommendation. Due to the amount of time that has elapsed, DCH informed us that it intends to implement reasonable collection efforts, but recognizes that these may have only limited success. Because of the age of the accounts, the accuracy and completeness of the records is not reliable. It is also possible that a number of these providers are no longer in business. In addition, DCH may have already collected the settlement amounts from some of the providers. The revenue reporting system used by the former Department of Mental Health did not track cash receipts to the individual contracts. At a minimum, the Accounting Division will send letters to providers requesting payment of the amounts due from cost settlement, or proof from the provider that payment was made. This will be completed by August 31, 1999. Additional or more aggressive collection efforts will be initiated, if necessary, based on materiality and by weighing the administrative cost of pursuing collection against the potential for these efforts to be successful.

FINDING

2. Cost Settlement Appeals

DCH did not resolve some appeals to its cost settlement of MORC's fiscal year 1992-93 and 1993-94 residential services contracts.

MORC entered into net cost contracts with its residential services providers for fiscal year 1992-93 and fiscal year 1993-94 (ended March 31, 1994). The DCH Central Office was responsible for cost settling these contracts at fiscal year-end and for hearing and resolving all related appeals. Cost settlement, the final reconciliation and adjustment of contractor revenues and expenditures, often resulted in contractors owing the State for amounts that MORC had overfunded them.

DCH accounting records indicated that 34 appeals, with a net amount due to the State of $497,634, were unresolved as of December 1, 1998. We reviewed 10 of these appeals totaling $255,534 and found that DCH had resolved 3 appeals prior to MORC's closing, 1 appeal had been litigated and resolved in 1998, and 1 appeal never existed. As of December 1, 1998, DCH had not attempted to resolve 5 of the appeals totaling $144,467. These appeals had been outstanding an average of 4.1 years.

DCH Administrative Directive 01-c-1116(j)-AD-17 requires a response to residential services providers' appeals within 14 days. We were informed that other priorities prevented the DCH staff person responsible for resolving the appeals from completing this responsibility. DCH cannot pursue collection of the amounts due to DCH for cost settlements in appeal until it resolves the appeals.

DCH would have increased the likelihood of collecting amounts due to the State if it had resolved the appeals prior to MORC's closure. This would have given DCH leverage to pursue collection while still having a continuing contractual relationship with the residential services providers. DCH's continued delays at resolving the appeals further reduce DCH's opportunity for collection.

RECOMMENDATION

We recommend that DCH resolve the appeals to its cost settlement of MORC's fiscal year 1992-93 and 1993-94 residential services contracts.

AGENCY PRELIMINARY RESPONSE

DCH agrees with the finding and recommendation. DCH informed us that by July 31, 1999, it will review the records for outstanding appeals, make an initial determination of the priority for resolution, and follow-up with each provider.

REAL AND PERSONAL PROPERTY

COMMENT

Audit Objective: To determine if DCH had adequate controls over MORC's real and personal property.

Conclusion: We determined that DCH had adequate controls over MORC's real property but did not have adequate controls over MORC's personal property. Our audit disclosed one reportable condition related to controls over personal property.

FINDING

3. Controls Over Personal Property

DCH did not establish an accurate and complete inventory record of the State-owned personal property in use by a private entity called Macomb-Oakland Regional Center, Inc. (MORC, Inc.). In addition, DCH did not establish the terms and conditions of the use arrangement in a written contract.

Prior to the closing, MORC's staff conducted a physical inventory of the State-owned personal property located at MORC. On September 28, 1996, MORC, Inc., continued to use MORC's State-owned personal property. DCH attempted to include the use of personal property in its building lease agreements with MORC, Inc. However, the Attorney General would not approve the leases, citing DCH's lack of statutory authority to include the personal property in the lease agreement. As a result, there was no contract establishing the terms and conditions of the use arrangement. This left the personal property without safeguards and at risk. The inventory listing prepared by MORC staff (now MORC, Inc., staff) was DCH's only comprehensive record of the State-owned personal property used by MORC, Inc.

During our March 1997 closing review of MORC, we tested the accuracy and completeness of this inventory listing. We reported that the inventory listing was

inaccurate and incomplete, and contained only generic descriptions of property items. Since our closing review, DCH had not completed a physical inventory of the personal property used by MORC, Inc. DCH initiated a physical inventory in February 1999, but had not completed it as of the end of our fieldwork. As a result, DCH still had not established an accurate and complete inventory listing of the personal property used by MORC, Inc. The Department of Management and Budget (DMB) Administrative Guide procedure 1270.05 requires DCH to physically inventory its equipment on an annual basis.

During our current audit, we attempted to locate 123 items included on the original inventory listing. We were unable to locate 25 items. MORC, Inc., informed us that it had discarded 5 of these items, traded in 1 item, and returned 1 item to DCH. MORC, Inc., could not account for the disposition of the remaining 18 items. MORC Inc., did not notify DCH that it had discarded or traded in the personal property items. As a result, DCH did not obtain DMB approval as required by DMB Administrative Guide procedure 340.05.

Although DCH cannot be assured that a newly compiled inventory record will accurately reflect all State-owned property in use by MORC, Inc., since September 28, 1996, it will provide the means for detecting future property losses. Ultimately, accurate inventory records, in conjunction with periodic physical inventories, help protect the State's assets. As of August 28, 1997, the appraised value of the personal property used by MORC, Inc., totaled approximately $110,000.

RECOMMENDATIONS

WE AGAIN RECOMMEND THAT DCH ESTABLISH AN ACCURATE AND COMPLETE INVENTORY RECORD OF THE STATE-OWNED PERSONAL PROPERTY IN USE BY MORC, INC.

We also recommend that DCH establish the terms and conditions of the use arrangement in a written contract.

AGENCY PRELIMINARY RESPONSE

DCH agrees with the findings and recommendations. DCH informed us that it has completed an accurate and complete inventory of all State-owned personal property currently in use by MORC, Inc. This inventory contains the physical description, condition, and location of each item. Each item has been identified

with unique State of Michigan tag numbers. DCH has also drafted a written use agreement for the personal property that has been reviewed and approved by the Department of Management and Budget. The draft agreement has been forwarded to MORC, Inc. for review and comment, and it is expected that the agreement will be fully executed by August 31, 1999.

EMPLOYEE TERMINATION SETTLEMENTS

COMMENT

Audit Objective: To determine if the termination settlements for MORC's employees were accurate.

Conclusion: We determined that the termination settlements for MORC's employees were generally accurate. However, our audit disclosed one reportable condition related to sick and annual leave payoffs.

FINDING

4. Sick and Annual Leave Payoffs

DCH did not ensure that MORC's employees were correctly paid for unused sick and annual leave upon retirement from MORC. In addition, DCH did not implement measures to mitigate control weaknesses related to the inadequate separation of duties over the processing of some MORC employee departure transactions.

Prior to MORC's closure, MORC staff prepared employee departure reports (form CS-301) for MORC's retiring employees and entered the information into the Personnel-Payroll Information System for Michigan (PPRISM). However, MORC staff incorrectly recorded the employees' departure date as October 1, 1996. The employees' last day of work at MORC, and therefore the departure date that MORC should have entered onto the CS-301 and into PPRISM, was September 27, 1996.

On October 1, 1996, PPRISM updated the hourly pay rate for all active classified State employees to reflect a pay increase approved by the Civil Service Commission. MORC's retiring employees received the pay increase because PPRISM considered the employees to be actively employed on this date.

Subsequent to the pay increase, PPRISM calculated and paid the retiring employees for unused sick and annual leave. In compliance with the Civil Service Compensation Plan, PPRISM calculated the payments based on the employees' last hourly pay rate. As a result, 30 retiring employees were overpaid a total of $7,112 because the pay rates had been erroneously increased.

DCH could have detected the errors in the CS-301's and prevented the overpayments by reconciling PPRISM's biweekly transaction report (PE-110) with the transaction source documents (i.e., CS-301's). The DCH Office of Human Resources informed us that, under normal conditions, MORC's personnel office would have reconciled the PE-110 with the transaction source documents. However, because MORC was closed, the Office of Human Resources should have completed the reconciliation. The Office of Human Resources informed us that it did not complete the reconciliation because of other staff priorities. The reconciliation would have also served as a compensating control to mitigate the control weakness related to MORC's inadequate separation of duties.

Two of the 9 CS-301's that we reviewed were prepared and entered by the same person, exemplifying MORC's inadequate separation of duties. In addition, 4 of the CS-301's did not note either the preparer or the entry person. As a result, we could not determine whether they had been prepared and entered by different people. We also noted that 3 of the CS-301's were not approved by the appointing authority. To ensure a proper separation of duties, PPRISM procedures preclude the same person from preparing, authorizing, and entering personnel transactions.

RECOMMENDATIONS

We recommend that DCH ensure that employees of closed facilities are correctly paid for unused sick and annual leave upon retirement.

We also recommend that DCH implement measures to mitigate control weaknesses related to the inadequate separation of duties over the processing of employee departure reports at closing facilities.

We further recommend that DCH collect all overpayments.

AGENCY PRELIMINARY RESPONSE

DCH agrees with the findings and recommendations. DCH is committed to making every possible effort to ensure staff in similar circumstances have proper training and direction to avoid these mistakes during any future closure activities. When a facility is closed, staff normally responsible for these personnel related duties frequently are transferred to other positions making it difficult to maintain a proper separation of duties. In the future, DCH will make every possible effort to maintain sufficient staff to ensure an adequate separation of duties. Every effort will also be made to ensure that all staff reassigned as a result of a future closure are trained in the transaction process. Transaction source documents (i.e., CS-301's - employee departure forms) will be reconciled to the biweekly transaction report (PE-110) as soon as possible for employees affected by a future closing. Finally, to the extent that it's administratively feasible and cost effective, reasonable efforts will be made to recoup the overpayments identified in the audit.

COMPLIANCE WITH LAWS, RULES, AND REGULATIONS

COMMENT

Audit Objective: To determine if DCH complied with selected laws, rules, and regulations in the closure of MORC.

Conclusion: We determined that DCH generally complied with selected laws, rules, and regulations in the closure of MORC. However, our audit disclosed one reportable condition related to conflict of interest.

FINDING

5. Conflict of Interest

DCH did not ensure that the MORC employees it assigned to leadership positions in the transition of service delivery from MORC to MORC, Inc., were free of conflicts of interest.

In July 1995, DCH initiated a process to transfer MORC's service delivery responsibilities to MORC, Inc. To guide the transition, DCH appointed key stakeholders to the MORC Futures Steering Committee. The Committee was responsible for developing an action plan that would, among other things, allow

MORC, Inc., to maintain stability and continuity of high quality services for MORC recipients and to preserve the body of expertise available through MORC. DCH appointed MORC's executive director and director of programs to the Committee. MORC's executive director served as the Committee's chairperson. DCH made these appointments with full knowledge that these individuals had incorporated MORC, Inc., in 1991 and served as directors of MORC, Inc. Also, upon the executive director's departure from MORC on June 1, 1996, DCH appointed MORC's director of programs to serve as MORC's acting director. This individual had given up his directorship of MORC, Inc., prior to this appointment but continued to maintain his business interest in MORC, Inc.

These individuals violated Section 2-21.1(e) of the *Rules of the Civil Service Commission* by simultaneously working in the aforementioned capacities. This section prohibits classified employees from representing or acting as an agent for any private interests in any transaction in which the State has a direct and substantial interest and which could reasonably be expected to result in a conflict between the private interests of the employee and the employee's official State responsibilities.

In addition, we noted instances when these employees violated Section 2-21.1(f) of the *Rules of the Civil Service Commission*. This section prohibits a classified employee from having a substantial interest in any business that the employee directly, in a significant decision-making capacity, participates on behalf of the State in the purchasing of any goods or services. For example, MORC's executive director compiled the expected operating costs of MORC, Inc., for fiscal year 1995-96 and submitted them to DCH for funding. DCH subsequently funded these operating costs, totaling approximately $3.2 million, through a contract with the Detroit-Wayne County Community Mental Health Agency. Although these conflicts existed, our audit disclosed no improprieties or irregularities on the part of the aforementioned individuals in completing their responsibilities related to the service transition.

In February 1996, a labor union representing MORC employees filed a conflict-of-interest complaint regarding these employees with the Department of Civil Service (DCS). Although DCH was aware of the complaint, it did not attempt to identify and eliminate any conflicts of interest. DCH could have sought, but did not seek, an advisory opinion from the State Ethics Board on whether any conflicts of

interest existed. In March 1999, DCS ruled that Sections 2-21.1(b),(e), and (f) were violated in the transition of services from MORC to MORC, Inc.

DCH informed us that it appointed MORC's executive director and director of programs to leadership positions in the transition to ensure continuity and consistency of services and to avoid problems encountered during the closure of other mental health facilities. DCH could have avoided the conflicts of interest by removing these individuals from their official positions at MORC. DCH could have used the knowledge and expertise of these individuals to ensure continuity and consistency of services through their participation on the Committee.

RECOMMENDATION

We recommend that DCH ensure that the State employees it assigns to leadership positions in the transition of service delivery from State control are free of conflicts of interest.

AGENCY PRELIMINARY RESPONSE

DCH agrees with the finding and recommendation. DCH acknowledges after the fact and does not dispute that the State personnel director found the circumstances involving these individuals and the transition of MORC into private hands constituted a per se violation of the *Rules of the Civil Service Commission*, Section 2-21. The investigation also concluded that there was no evidence that any of the principals misused their State authority or compromised any interest of the State as a result of their interest in MORC, Inc. In order to ensure a smooth transition with little or no disruption in service responsibilities, DCH created a committee to examine all aspects of the process transferring the operation from the State to MORC, Inc., a private entity. As part of the process, a steering committee was established which included the then facility director and program director. These appointments were made in an effort to include persons with intimate knowledge of the facility operations in the decision making process.

To ensure that similar conflicts are avoided in the future, DCH informed us that it has implemented the recommendation made by the State personnel director by reviewing and implementing its conflict of interest work rules. These new rules were issued June 16, 1999 and took immediate effect.

RECIPIENT RIGHTS

COMMENT

Audit Objective: To determine if DCH ensured that the rights of MORC's recipients were protected subsequent to the closure of MORC.

Conclusion: We determined that DCH ensured that the rights of MORC's recipients were protected subsequent to the closure of MORC.

Noteworthy Accomplishment: DCH, in conjunction with the Detroit-Wayne, Oakland, and Macomb county community mental health services programs, and MORC, Inc., directed the transition of MORC's service delivery system from MORC to MORC, Inc., in approximately 12 months. Throughout the transition, DCH ensured active family and recipient involvement in service planning, stability in the areas of housing, community, relationships, support systems, and funding. As a result, DCH accomplished the transition with little or no disruption in services to the recipients. The transition required, among other things, the assurance of a stable work force of over 350 employees, the transfer of responsibility for over 2,000 recipients, and the conversion of all functions associated with operating MORC. Some of these functions, including (but not limited to) accounting, financial reporting, and payroll and personnel, required extensive development because the State had provided the functions prior to the transition.

Glossary of Acronyms and Terms

conflict of interest	A conflict between the private interests and public obligations of a person in an official position.
cost settlement	The final reconciliation and adjustment of contractor revenues and expenditures.
DCH	Department of Community Health.
DCS	Department of Civil Service.
developmentally disabled	A condition that become evident in childhood; is expected to continue indefinitely; constitutes a substantial handicap to the affected individual; and is attributed to mental retardation, cerebral palsy, epilepsy, or other neurological conditions.
DMB	Department of Management and Budget.
effectiveness	Program success in achieving mission and goals.
efficiency	Achieving the most outputs and outcomes practical for the amount of resources applied or minimizing the amount of resources required to attain a certain level of outputs or outcomes.
housing development services	The establishment of a residential setting, including homes, condominiums, and apartments, for the placement of recipients.
internal control structure	The management control environment, management information system, and control policies and procedures established by management to provide reasonable assurance that goals are met; that resources are used in compliance with laws and regulations; and that valid and

reliable performance related information is obtained and reported.

material condition A serious reportable condition which could impair the ability of management to operate a program in an effective and efficient manner and/or could adversely affect the opinion of an interested person concerning the effectiveness and efficiency of the program.

mentally ill A condition involving a substantial disorder of thought or mood that significantly impairs the individual's judgment, behavior, capacity to recognize reality, or ability to cope with the ordinary demands of life.

MORC Joseph M. Snyder Macomb-Oakland Regional Center.

MORC, Inc. Macomb-Oakland Regional Center, Incorporated.

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 public accountability and to facilitate decision making by parties responsible for overseeing or initiating corrective action.

personal property equipment and furnishings.

PPRISM Personnel-Payroll Information System for Michigan.

real property land and buildings.

recipients Individuals receiving mental health services.

reportable condition A matter coming to the auditor's attention that, in his/her judgment, should be communicated because it represents either an opportunity for improvement or a significant

deficiency in management's ability to operate a program in an effective and efficient manner.

residential services Services provided in residential settings which may include room and board, 24-hour supervision and protection, and specialized mental health services in-home or out-of-home. These services are designed to enhance the health, welfare, and development of a recipient with developmental disabilities or mental illness.

review A level of service lower than an audit conducted in accordance with the American Institute of Certified Public Accountants' Standard for Accounting and Review Services. A review differs from an audit in that many audit procedures required by an audit are not required to be conducted during a review.