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INDEPENDENT STATE AUDITOR'S
REPORT ON CERTAIN ACTIVITIES
OF THE
CENTER FOR HEALTH AND DEVELOPMENT, INC.
JULY 1, 1997 THROUGH JUNE 30, 2000

OFFICIAL AUDIT
REPORT
AUGUST 16, 2001

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The Center for Health and Development, Inc., (CHD) was incorporated in 1987 as a private, not-for-profit corporation. CHD provides a variety of services, including psychiatric treatment and rehabilitation services, training and technical assistance, residential services, and community support services, to eligible individuals throughout the Commonwealth. Our audit, which covered the period July 1, 1997 to June 30, 2000, had the following objectives: (1) determine whether CHD had established an adequate system of management controls and (2) assess CHD's business practices and its compliance with applicable laws, regulations, and policies and procedures and various fiscal and programmatic requirements of its state contracts. Our audit identified at least \$142,488 in questionable, unreasonable, and undocumented expenses; \$44,685 in unnecessary conference expenses; inadequate controls over \$440,599 in consultant services, \$275,869 in fixed assets inventory, and agency personnel and time and attendance records; inadequate board oversight; and an undisclosed related party transaction totaling \$3,896.

AUDIT RESULTS

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INTRODUCTION

Background

The Center for Health and Development (CHD) was founded in 1987 as a not-for-profit corporation to provide forensic mental health services to eligible individuals throughout Massachusetts. CHD currently offers the following programs and services:

Adult Residential Services: Since July 1987, CHD has been providing residential services serving individuals diagnosed with serious mental illness. During the period of our audit, CHD operated six residential programs located in Framingham, Weymouth, Fitchburg, Leominster, Winchendon, and Wakefield that housed approximately 87 clients. CHD works with individuals in these programs to assist them in achieving their goals and objectives and performing their daily activities.

Clubhouse Programs: CHD operates two Community Support Clubhouses (Clubhouse Programs) located in Quincy and Wakefield. The Clubhouse Programs support individuals by teaching them skills that allow them to move towards independence in the areas of employment, housing, education, and social skills.

Day Rehabilitation Program: CHD operates its day rehabilitation program, or ALPHA Program, in the Metropolitan Boston area. This program is designed to provide a supportive environment for individuals with mental illness by teaching them new skills and coping techniques. CHD provides assistance to individuals in acquiring and maintaining mental, physical, and social skills that enable them to function effectively.

Vocational Rehabilitation Services: Since 1991 CHD has been under contract with the Massachusetts Rehabilitation Commission (MRC) to provide vocational rehabilitation services to individuals with psychiatric disabilities. CHD provides vocational evaluation, work adjustment training, job support services, and supplemental support services. Currently, CHD provides these services in the North East Suburban and Metro Boston areas.

Forensic Mental Health Services: During the period of our audit, CHD provided forensic mental health evaluations, education, consultation, disposition, and referral services for persons with serious mental health problems who come before the courts. This service ensures that persons with serious or long-term mental health problems are offered the comprehensive services they need and that those without serious forensic mental health problems are responded to appropriately by the courts. For several years, CHD provided forensic mental health services in 40 district courts and county correctional facilities located throughout the Commonwealth. However, as of July 1, 1999, CHD was providing these services only to courts located in central Massachusetts, specifically the Worcester Superior Court and the district courts located in Westboro, East Brookfield, Dudley, Uxbridge, Milford, Fitchburg, Leominster, Gardner, Ayer, Clinton, and Winchendon.

CHD's funding primarily comes from state funds. For fiscal years 1998 through 2000, CHD received the following revenues:

The Center for Health and Development, Inc.
Summary of Revenues
Fiscal Years 1998 through 2000

	<u>Fiscal Year</u> <u>1998</u>	<u>Fiscal Year</u> <u>1999</u>	<u>Fiscal Year</u> <u>2000</u>
<u>Revenue – Government</u>			
Department of Mental Health (DMH)	\$5,109,482	\$5,143,625	\$3,944,360
Department of Mental Retardation (DMR)	556,891	397,536	-
Department of Public Health (DPH)	122,455	227,028	205,536
Massachusetts Rehabilitation Commission (MRC)	41,130	22,660	32,208
Client Resources (SSI/Food Stamps)	174,628	203,325	196,102
<u>Revenue – Other</u>			
Subcontract – Mass. Government	-	3,000	3,000

	<u>Fiscal Year</u> 1998	<u>Fiscal Year</u> 1999	<u>Fiscal Year</u> 2000
Gifts, Contributions, Legacies	-	-	2,260
Free Use of Assets –			
Capital Budget	25,739		
Private Grant –	24,025	17,580	19,269
Unrestricted			
Investment Revenue	2,332	3,729	4,616
Private Contract	4,850	-	
Other Unrestricted			
Revenue	<u>-</u>	<u>63,280</u>	<u>19,885</u>
Total Revenue	<u>\$6,061,532</u>	<u>\$6,085,723</u>	<u>\$4,431,729</u>

Audit Scope, Objectives, and Methodology

The scope of our audit was to examine certain administrative and fiscal activities of CHD during the period July 1, 1997 to June 30, 2000. Our audit was conducted in accordance with applicable generally accepted government auditing standards for performance audits and included procedures and tests considered necessary by the Office of the State Auditor to meet these standards.

Our audit objectives consisted of the following:

1. A determination of whether CHD has established and implemented adequate and effective management controls, including:
 - Policies and procedures to ensure internal administrative and accounting controls over CHD revenues, expenses, and fixed assets;
 - Processes for planning, organizing, directing, and controlling program operations;
 - Policies and procedures to ensure that resource use is consistent with laws and regulations; and
 - Policies and procedures to ensure those resources are safeguarded and efficiently used.
2. An assessment of CHD's business practices and its compliance with applicable laws, rules, and regulations as well as the various fiscal and programmatic requirements of its state contracts.

In order to achieve the audit objectives, we first assessed the system of management controls established and implemented by CHD over its operations. The purpose of this assessment was to obtain an understanding of management's attitude, the control environment, and the flow of transactions

through CHD's accounting system. The assessment was used in planning and performing our audit tests. We then held discussions with CHD officials and reviewed organizational charts and internal policies and procedures. We also reviewed all applicable laws, rules, and regulations. Finally, we examined CHD's financial statements, budgets, cost reports, invoices, and other pertinent financial records to determine whether expenses incurred under CHD's state contracts were reasonable, allowable, allocable, properly authorized and recorded, and in compliance with all applicable laws, rules, and regulations.

Our review was not made for the purposes of forming an opinion on CHD's financial statements. We also did not assess the quality and appropriateness of program services provided by CHD through its contracts. Rather, our report was intended to report findings and conclusions regarding CHD's compliance with applicable laws, rules, and regulations; the adequacy of CHD's performance; and specific processes, methods, and internal controls that could be made more efficient and effective.

AUDIT RESULTS

1. Unreasonable and Unnecessary Board Expenses Totaling at Least \$24,651, Board Members Not Effectively Performing Their Oversight Responsibilities, and Questionable Compensation and Fringe Benefits Totaling \$16,441 Provided to the Agency's Former Executive Director

Our review of the Center for Health and Development (CHD) revealed that seven of the agency's eight board members are not Massachusetts residents. As a result, the agency's board is unable to effectively meet all of its required oversight responsibilities. We also found that the agency incurred as much as \$24,651 in unnecessary board expenses, including charging for teleconferencing equipment, transportation, hotels, and meals for its out-of-state board members to attend board meetings. Moreover, we found that, although during our audit period CHD's former Executive Director received \$16,441 in pay increases and additional fringe benefits, there was no written documentation to substantiate that CHD's Board of Directors authorized this additional compensation and benefits.

The Board of Directors of CHD is the primary organizational body that ensures that CHD meets its operational objectives in the most effective and efficient manner. Board members perform a variety of key functions, including overseeing the overall operation of the agency, setting policies and procedures to ensure that agency objectives are met, and hiring the agency's top executive. Chapter 180, Section 6A, of the Massachusetts General Laws, commonly referred to as the Public Charities Law, empowers not-for-profit organizations such as CHD to make, amend, and repeal bylaws that prescribe the number, term, powers, and responsibilities of its Board of Directors, officers, and Executive Director. In addition, the state's Executive Office for Administration and Finance, Operational Services Division (OSD), has promulgated Terms and Conditions for Human and Social Service Contracts (General Contract Conditions), with which all human service providers which contract with state agencies must comply. Regarding an agency's Board of Directors, Condition 11 of these General Contract Conditions states:

If a non-profit organization, the Provider will comply with the principles contained in the Massachusetts Attorney General's "Guide for Board Members of Charitable Organizations" and with the standards for boards contained in the AICPA's [American Institute of Certified Public

Accountants] statement on auditing standards, as may be amended from time to time. Further, the Provider specifically agrees to the following:

- The Provider's board of directors will, on an annual basis, review its Executive Director's or other most senior manager's performance and set the person's compensation by a formal vote;
- The provider's board of directors will meet as frequently as necessary to fulfill the Provider's obligations under this section. Where the board meets less than two times during the fiscal year, the Provider shall submit a description of its board structure and the dates of each board and subcommittee meeting with its UFR.

As described below, during our audit we found a number of problems relative to CHD's Board of Directors.

Ineffective Board Oversight and Unreasonable and Unnecessary Board Expenses Totaling at Least \$24,651: Typically, members of an agency's Board of Directors reside in the communities being served by their organization, which allows board members to be cognizant of the issues affecting their organization within the community, and provide the oversight necessary to ensure that agency objectives are met in the most efficient and effective manner. During the period of our review, we noted that seven of CHD's eight board members resided not in Massachusetts but in other states and countries, including New Jersey; Maryland; Washington, D.C.; Georgia; Illinois; and Johannesburg, South Africa. One board member splits his time between Somalia and Maryland. This geographic dispersion of the board members limits the amount of direct contact they have with each other as well as with agency staff. As a result, most of the administrative functions involving CHD's board was being performed by CHD's only local board member. This condition also makes it difficult for CHD to conduct agency business in an effective and expeditious manner.

For example, in January 1997, CHD's board voted to establish an Executive Committee that would meet once a month via teleconference to remain current with CHD's day-to-day business operations. However, we found that, due to the unavailability of board members, the Executive Committee was able to teleconference only eight times during the three-year period of our audit. Also, although CHD drafted

a new version of its Policy and Procedures Manual in July 1999, CHD officials told us that as of the end of our audit fieldwork, the board has not been able to get together to approve this manual. Moreover, in January 1999, CHD's former Executive Director requested that the board's Executive Committee authorize the hiring of a part-time contract manager to help complete a proposal that would allow CHD to continue to provide forensic mental health services to the Department of Mental Health (DMH) consumers. Due to a lack of communication and its lack of awareness of the day-to-day operations of CHD, the agency's Executive Committee never acted upon this request. Subsequently, CHD lost 75% of its original forensic mental health contract with DMH, which amounted to approximately \$1.8 million in annual funding to the agency.

This dispersion of board members also caused CHD to incur unreasonable costs in that the agency pays for food, lodging, and transportation expenses board members incurred for attending meetings and for the rental of teleconferencing equipment when they need to discuss various matters. During our three-year audit period, CHD's board met four times, including one meeting that was held in Maryland, and twice held meetings via teleconferencing. The total cost of these meetings and teleconferencing sessions was \$24,651, which CHD charged against its state contracts. The table below summarizes these expenses:

Center for Health and Development, Inc.
Summary of Expenses of the Board of Directors
Fiscal Years 1998 through 2000

<u>Fiscal Year</u>	<u>Number of Meetings</u>	<u>Travel/Food Lodging</u>	<u>Teleconferencing</u>	<u>Total</u>
1998	One	\$11,628	\$ 621	\$12,249
1999	Two	3,534	677	4,211
2000	One	7,340	851	8,191
		<u>\$22,502</u>	<u>\$2,149</u>	<u>\$24,651</u>

The state's Operational Service Division (OSD), the agency responsible for regulating the purchase of services from human services organizations such as CHD, has promulgated regulations that specifically identify costs that are nonreimbursable under state contracts. In this regard, 808 Code of

Massachusetts Regulations (CMR) 1.05(1) promulgated by OSD identifies the following as a nonreimbursable cost:

Unreasonable Costs. Any amount paid for goods or services which is greater than either the market price or the amount paid by comparable Departments or other governmental units within or outside of the Commonwealth.

Had the agency used individuals from within the Commonwealth to serve on its board, as in the case with the vast majority of the human service organizations that the Office of the State Auditor has audited, the agency would not have incurred the \$24,651 in unreasonable board-related expenses. Moreover, these funds would then have been available to provide needed services to CHD's consumers.

Noncompliance with Applicable Guidelines and Contractual Terms and Conditions Relative to CHD's Board of Directors and Questionable Compensation and Fringe Benefits Totaling \$16,441: As previously noted, the state's General Contract Conditions require an agency's Board of Directors to annually review its Executive Director's performance and set this person's compensation by formal vote. Additionally, the state's Office of the Attorney General has published guidelines on the duties and responsibilities of members of the Board of Directors of not-for-profit organizations. According to these guidelines, the "process for setting CEO compensation, the amount of such compensation, and the terms of such compensation should all be approved by the full board and be sensitive to public concerns." During the period of our review, the agency's former Executive Director received an increase in salary of 8% effective October 7, 1998, amounting to an additional \$8,704 during the period of our audit, an increase of two weeks in paid leave time with a value of \$3,605 during the period of our audit, and additional fringe benefits of \$4,132 in annual paid parking expenses. Our review of the minutes of CHD's Board of Directors, including the minutes of the agency's Executive Committee meetings conducted during our audit period, did not indicate that an annual review of the former Executive Director's performance had been performed in order to justify this additional compensation. Further,

there was no documentation to substantiate that the board had authorized this additional compensation and benefits.

In addition, according to Condition 7 of the state's General Contract Conditions, CHD is required to have a written policy regarding nepotism. During the period of our review, we discovered documentation from the agency's Board of Directors addressed to the agency's former Executive Director requesting that a nepotism policy be drafted before his departure in March 2000. However, as of the end of our audit fieldwork, no nepotism policy had been drafted.

Also, CHD's corporate bylaws require that the Clerk of the board attend all meetings of the corporation and record and maintain records of all proceedings of the Board of Directors. However, during our audit we found that, of the four regular board meetings held, only three indicated who was in attendance and of the eight executive sessions held, only three indicated who was in attendance. Two executive session meetings included the agenda for the meeting but did not include any minutes of the meeting. Therefore, what was discussed at these meetings could not be determined. Furthermore, the authenticity of the minutes was not certified by the Clerk, and the preparer of the minutes was not identified.

CHD officials stated that they had spoken to the board regarding our concerns relative to the maintenance of board minutes, and these officials told us that in the future, the board would prepare minutes for all of its meetings. However, these officials did not comment on our other concerns relative to this matter.

Recommendation: In order to address our concerns relative to matter, CHD's principal state purchasing agency, DMH, should recover the \$24,651 in unreasonable board expenses and the \$16,441 in questionable compensation and fringe benefits provided to the agency's former Executive Director. Additionally, DMH should conduct a review of the board-related expenses charged by CHD against its state contracts for the periods prior and subsequent to our audit period and based on this review, should

recover whatever funds it deems appropriate. In the future, CHD should take the measures necessary to ensure that the composition and activities of its Board of Directors comply with the requirements of state regulations and the guidelines issued by the Office of the Attorney General. Further, the agency should consider reconstituting its board to include local residents.

Auditee's Response: In response to this audit result, CHD officials provided the following comments:

We have always considered it a plus that our Board of Directors brings invaluable expertise and understands directly, from their own experience, the issues we deal with serving our consumers on a daily basis. Originally, all of the members of our Board of Directors were located in the Commonwealth. They conceived the idea of developing an organization that would focus its energies on serving unserved or underserved individuals, families or grassroots organizations and support them to be self sustaining contributors in the communities they are a part of. . . .

The [audit report's] claim of only eight Executive Committee meetings over the three-year period is incorrect. There were at least twelve meetings of the Executive Committee of the Board of Directors during that period. Additionally, the whole Board met at least four times.

The [audit report's] assertion that the [Executive Committee] EC denial of a request to hire a part time contract manager is also incorrect. A reading of the minutes from the January 29, 1999 EC meeting, details a discussion of the Forensic Contract, whereby the EC is not only supportive of efforts to bring additional talent on board, but was prepared to interview candidates. The . . . attempt to lay blame for the loss of a portion of the Forensic Contract, which ultimately was awarded to the University of Massachusetts Medical School, at the feet of the EC, is groundless.

In the comments about the Board's geographic make-up, the audit fails to take into account the mission of CHD, as articulated by the Board in the organization's Mission Statement. CHD is committed to provide services to communities not only in Massachusetts, but also in the southern United States, the Caribbean and Africa. The audit is attempting to define a non-profit by the programs and contracts it has, rather than by the stated Mission of the organization.

The [audit report] has classified all Board related expenses incurred within the audit period as "unreasonable" and therefore non-allowable. The audit has made this determination on the basis that the majority of the Board are not residents of the Commonwealth. CHD is not aware of any MGL or regulation of the Attorney General that requires boards of directors to have a specific geographic or any other requirement. The audit paraphrases CMR 808 Section 1.05(1), which provides a definition of unreasonable costs. However, the audit fails to quote Section 1.05(1) in its entirety. . . .

Unreasonable Costs. Any costs not determined to be Reasonable Operating Costs as defined in 808 CMR 1.02 or any amount paid for goods or services which is greater than either the market price or the amount paid by comparable Departments or other governmental units within or outside of the Commonwealth."

In fact, CMR 808 Section 1.02 specifically defines "general board activities" as allowable administrative and support costs. Furthermore, boards of directors cannot be obtained by competitive bidding, like lawyers, CPA's or cleaning companies, therefore, having no comparative market value as intended by this regulation. Additionally, the term "Departments" as used in this section is defined in CMR 808 1.02 as:

"Department. Any Executive Office, Department, Agency, Office, Division, Board, Commission or Institution within the Executive Branch, excluding the Legislative Branch, Judicial Branch, Constitutional Offices, Elected Officials, Public Institutions of Higher Education, the Military Division and Independent Public Authorities. ..."

We are not aware of boards of directors for any of these departments or governmental units to measure the Board costs of CHD against. Furthermore, CMR 808 1.02 goes on to define reimbursable operating costs as:

"Reimbursable Operating Costs. Those costs reasonably incurred in providing the services. . . Operating costs shall be considered "reasonably incurred" only if they are reasonable and allocable using the standards contained in Federal Office of Management and Budget Circular A-122 or A-21, or successors thereto."

Office of Management and Budget (OMB) Circular A-122, revised June 1, 1998, specifically states under Trustees' Travel. . . .

OMB concurs that disallowing the reimbursement of trustees' travel costs could inhibit the recruitment of qualified Board members (particularly at smaller non-profit organizations), thereby hampering the operations of a non-profit organization. OMB also recognizes that trustees travel costs are reasonable and necessary business costs. As a result, trustees' travel costs remain allowable.

The [audit report's] assertion that Board costs are "unreasonable" is purely subjective. The audit has not offered any qualitative evidence to support this claim. This position is also not supported by Federal regulation or any regulation of the Commonwealth. Additionally, by classifying board costs as "unreasonable", the audit is not only attempting to place a value on the members of boards of directors, but is also attempting to regulate how boards of directors are formed.

Additionally, during the past two years there has been a focus by CHD's Board to bring in local expertise to increase the ability for the Board to have additional involvement in the day to day running of CHD. This process included the development of local Advisory Councils for each program type, with a set of approved by-laws. Finally, the Board also voted to bring on new members who reside in the Commonwealth and have developed a committee focused on the completion of this process.

Regarding the former Executive Director compensation and benefit package, our research shows that indeed there was a process conducted by the Board to increase [the former Executive Director] salary and vacation time. In March of 1998 [the former Executive Director] raised the issue at a Board Meeting and was told that [the] chairman of the Board would coordinate the process for his evaluation by the Board and the Senior Management Team. A memo went out to

both groups asking them to fill out an evaluation form rating [the former Executive Director]. Upon receiving the feedback, the Board recommended [the former Executive Director] receive an 8% raise as he received no additional compensation during the prior year. Additionally at that time they agreed to increase [the former Executive Director's] vacation time to 4 weeks per year. Parking was not considered a part of a benefit package but has been afforded to all Senior Managers of CHD as a part of conducting business for the company. Since all Senior Managers, including the Executive Director travel a great deal to the programs across the Commonwealth they need to have their car accessible to them at all times. The authorization for all raises at CHD is in the form of an Employee Human Resources change form which document any change in salary, allocations, etc. and must be signed by the appropriate CHD manager or in this case the President of the Board. The CHD Board President signed the change form so the adjustment could be processed through CHD's personnel and payroll system.

Auditor's Reply: We acknowledge the fact that originally all of the members of CHD's Board of Directors were located in the Commonwealth. Apparently, CHD recognized then the importance of having local individuals on its board. Further, we do not argue the fact that certain members of CHD's Board of Directors have valuable expertise. However, our concern is that given its geographic dispersion, the board clearly cannot meet all of its oversight responsibilities. As stated in our report, in January 1997, CHD's board voted to establish an Executive Committee that would meet once per month via teleconferencing to remain current with CHD's day-to-day operations. However, based on the documentation provided to us by CHD officials, the Executive Committee was able to teleconference only eight times during the 36-month period of our audit. If, as CHD contends in its response, the Executive Committee actually teleconferenced at least 12 times during this three-year period, the agency was not able to provide us with any documentation to substantiate this fact. Based on CHD's response that "there were at least twelve meetings of the Executive Committee ... clearly the agency is unsure of the actual number of times the Executive Committee met. Moreover, even if the Executive Committee met 12 times during our audit period as CHD claims, this number represents one-third of the times that CHD's Board of Directors believed was necessary to effectively oversee the day-to-day operations of the agency.

The minutes of the January 29, 1999 meeting of CHD's Executive Committee does not indicate that it was in the process of hiring or even considering to hire a part-time contract manager. While these

minutes do indicate that CHD was in the process of hiring new staff, there was no mention of a contract manager. As stated in our report, the documentation provided to us by CHD officials clearly indicates that the Executive Committee did not approve the hiring of a contract manager, which contributed to the agency losing 75% (approximately \$1.8 million in annual funding) of its forensic mental health contract. Since the Executive Committee was officially charged by CHD's Board of Directors to oversee its day-to-day operations, we believe it is appropriate to hold the Executive Committee accountable to this matter.

Despite the fact that CHD's mission statement states that it may provide services to communities outside Massachusetts, CHD has been in operation for over 14 years and has never operated any programs in the areas where current board members are located. Moreover, during fiscal years 1998, 1999, and 2000, 96.6%, 95.2%, and 94.5%, respectively, of CHD's total funding came from Massachusetts state contracts, indicating that CHD had no intention, at least in the near term, to expand its operations into other geographic locations. We are not, as CHD contends in its response, attempting to "define" CHD by its programs and contracts. Rather, we are merely questioning the necessity of having board members reside in geographic areas where the agency operates no programs and receives no funding. Based on the documentation we reviewed, clearly the geographic dispersion of CHD's Board of Directors causes CHD to incur unnecessary costs and limits the board's ability to effectively perform its oversight responsibilities.

For the reasons mentioned, we strongly believe that many of the board's related costs (e.g., travel and lodging) were unnecessary and, therefore, unreasonable. We agree with CHD that OMB Circulars recognize that certain board expenses are necessary and allowable. However, all expenses, including board expenses, must be reasonable in order to be allowable. While state regulations characterize unreasonable terms of relative costs, federal guidelines with which CHD must comply define unreasonable costs in a broader context. Specifically, OMB Circular A-122 characterizes unreasonable

costs as "costs, which do not effect the actions a prudent person would take in the circumstances." We do not believe that it is prudent for an agency to incur the expenses of board members to travel, in some instances, thousands of miles to attend meetings or to hold teleconference meetings when it has not made reasonable efforts to obtain local representation on its board. We believe that CHD should have used these funds for providing services to its needy consumers.

As stated in our report, CHD did not provide us any documentation to substantiate that an annual review had been performed on CHD's former Executive Director that would justify the additional compensation he was provided during our audit period. Although we requested the minutes of all board and EC meetings during our audit period, we were not provided with any minutes from a March 1998 meeting that CHD refers to in its response. In addition, upon review of the former Executive Director's personnel folder, the only indication of the increase in pay was indicated by the HR Information Form. Evaluations conducted by the board were not provided nor attached to the HR Form. In addition, the increase in vacation time was not stated on the HR Form.

As discussed under Audit Result No. 2, and in response to the parking benefit, we stated the need to adopt a formal travel policy numerous times during our review of CHD. The former Executive Director agreed with this need and stated that the travel policy would be drafted. In addition, upon review of the board minutes, the board recognized the need for a formalized travel policy. Consequently, CHD does not have a formalized travel policy and, therefore, the benefit is unallowable.

2. Undocumented, Inadequately Documented, and Non-Program-Related Expenses Totaling \$39,972 and Potentially Excessive Conference Costs Totaling at Least \$44,685

We found that \$39,972 in expenditures that CHD charged against its state contracts during the period of our audit were undocumented, inadequately documented, or unsubstantiated by the agency with adequate documentation detailing how these expenses benefited its state programs. According to state regulations, expenses such as these that are not properly documented or non-program-related are unallowable and nonreimbursable under state contracts. We also found that CHD did not have any

policies relative to staff members attending conferences. As a result, CHD incurred at least \$44,685 in potentially excessive conference costs, including having as many as 13 employees attend the same conference.

The 808 Code of Massachusetts Regulations (CMR) 1.05(3)(d), (12), and (26) promulgated by OSD identifies the following as nonreimbursable costs under state contracts:

(3)(d) Certain Interest. Any interest or penalties incurred because of late payment of loans or other indebtedness. . . .

(12) Non-Program Expenses. Expenses of the Contractor which are not directly related to social service program purposes of the Contractor.

(26) Undocumented Expenses. Costs which are not adequately documented in the light of the American Institute of Certified Public Accountants statements on auditing standards for evidential matters.

During our audit, we found that the following expenses billed by CHD against its state contracts were not in compliance with these regulations.

Questionable Credit Card Expenditures Totaling \$32,585: During our audit period, CHD allowed seven members of its administrative staff, including the agency's former Executive Director, to use agency American Express credit cards. During our audit, we reviewed the documentation maintained by CHD relative to all of the 1,897 credit card expenditures totaling \$315,581 that CHD charged against its state contracts during the three fiscal years of our audit. Our review revealed purchases totaling \$32,585 that were either undocumented, inadequately documented, or non-program-related and non-reimbursable under CHD's state contracts, as shown in the following tables:

Center for Health and Development, Inc.
Summary of Unallowable Credit Card Expenses
Fiscal Years 1998 through 2000

	<u>Fiscal Year</u> 1998	<u>Fiscal Year</u> 1999	<u>Fiscal Year</u> 2000	<u>Totals</u>
Inadequately Documented	\$4,224	\$ 3,409	\$5,922	\$13,555
Undocumented	550	1,244	-	1,794
Non-Program-Related	<u>3,883</u>	<u>6,353</u>	<u>7,000</u>	<u>17,236</u>
	<u>\$8,657</u>	<u>\$11,006</u>	<u>\$12,922</u>	<u>\$32,585</u>

The nature of these \$32,585 in expenses are as follows:

<u>Description</u>	<u>Fiscal Year</u> 1998	<u>Fiscal Year</u> 1999	<u>Fiscal Year</u> 2000	<u>Totals</u>
Meals	\$4,224	\$3,409	\$5,922	\$13,555
No Receipts	550	1,244	-	1,794
Gifts	589	822	445	1,856
Flowers	651	220	257	1,128
Cakes	108	89	-	197
Parking	2,535	4,890	6,161	13,586
Late Charges	-	131	137	268
Other	-	<u>201</u>	-	<u>201</u>
	<u>\$8,657</u>	<u>\$11,006</u>	<u>\$12,922</u>	<u>\$32,585</u>

Examples of these undocumented, inadequately documented, and non-program-related expenses follow.

- During the period of our review, CHD made purchases of \$1,794, for which no documentation exists.
- We identified 57 purchases for food and beverages totaling \$13,555 that were inadequately documented and therefore nonreimbursable. For example, most of the expenses did not indicate who attended the meals, the business purpose of the meal, or how state-funded programs benefited from the meal. Some examples of these expenses include: on October 8, 1998, a meal at Jae's in Boston costing \$296.33 was charged by the former Executive Director with no explanation as to its business nature; on November 25, 1998, a meal for \$115 was charged for a going-away celebration at the Omni Parker House with no explanation as to its business nature; and on August 18, 1999, a charge for \$165.45 at Strip-T's and Buzz was also charged by the former Executive Director with no explanation as to its business nature.

- During the period of our audit, CHD expended \$1,128 for flowers. Since this expense is personal in nature, it should not have been charged by CHD against its state contracts.
- During each of fiscal years 1998, 1999, and 2000, CHD held an annual holiday party. The total expense for the three years was \$7,476. (\$4,024 for fiscal year 1998, \$1,410 for fiscal year 1999, and \$2,042 for fiscal year 2000). In addition, during fiscal year 2000, CHD held a going away party for its former Executive Director. The total cost of this party, including \$225 for a jazz band, was \$1,994. CHD charged all of these costs against its state contracts. However, since these are non-program related costs, they are nonreimbursable under CHD's state contracts.
- We identified 11 late charges and/or interest charges during fiscal years 1998, 1999, and 2000 for a total of \$268, which is unallowable under 808 CMR 1.05(3)(d).
- During fiscal year 1999, CHD made nine payments for internet service accounts, totaling \$201. According to CHD officials, these accounts were not for business purposes, and therefore, CHD should not have charged this expenses against its state contracts.
- During the period of our audit, CHD purchased various gifts totaling \$1,856. However, the agency did not have any documentation indicating who received these gifts or how these gifts were used to benefit consumers in CHD's state-funded programs.
- We identified \$13,586 in parking expenses that CHD officials said were for its employees. However, these receipts did not state the business purpose of the expense or who received the benefit.

Other Questionable Expenses Totaling \$7,387: In addition to the unallowable credit card expenses discussed above, during our audit we also reviewed a sample of the documentation being maintained by CHD relative to \$83,366 in non-credit-card expenses charged by CHD against its state contracts during our audit period. Based on our review, we noted \$7,387 of these purchases were either inadequately documented or appeared to be non-program-related, as shown in the following summary:

	<u>Fiscal Year</u> <u>1998</u>	<u>Fiscal Year</u> <u>1999</u>	<u>Fiscal Year</u> <u>2000</u>	<u>Totals</u>
Inadequately Documented	\$ 746	\$2,667	\$1,559	\$4,972
Undocumented	-	-	50	50
Non-Program-Related	<u>814</u>	<u>806</u>	<u>745</u>	<u>2,365</u>
	<u>\$1,560</u>	<u>\$3,473</u>	<u>\$2,354</u>	<u>\$7,387</u>

Examples of these questionable expenses follows:

- During the period of our audit CHD expended \$963 for flowers. Since these expenses were personal in nature they should not have been charged against CHD's state contracts.

- CHD charged \$4,972 against its state contracts for "meeting expenses." However, the documentation maintained by CHD relative to these expenses did not state the business purpose of the meeting or identify which CHD staff attended these meetings.
- During the period of our audit, we noted \$1,097 in other unallowable expenses, including \$406 paid to Federal Express, to send packages to the former Executive Director who was living in South Carolina after his last date of employment with CHD; \$520 for a down payment for a holiday party in 1998; and \$85 expended for parking tickets incurred by CHD employees, of which \$39 was paid for employee parking and \$46 was charged directly to state program for a Day Timer for a staff member.

Potentially Excessive Conferences Expenses Totaling at Least \$44,685: As previously mentioned, OSD regulations state that any costs that are deemed to be unreasonable are nonreimbursable under state contracts. During our audit period, CHD sent a number of its employees to three major conferences. The expenses for these three conferences totaling \$44,685, which CHD charged against its state contracts, are shown below:

Center for Health and Development Inc.

Summary of Conference Costs

Fiscal Years 1998 through 2000

<u>Description</u>	<u>Fiscal Year 1998</u>	<u>Fiscal Year 1999</u>	<u>Fiscal Year 2000</u>	<u>Totals</u>
Airline Tickets	\$2,030	\$3,967	\$1,119	\$7,116
Registration	3,600	3,820	3,590	11,010
Hotel Expenses	7,109	6,657	6,753	20,519
Meals	2,282	1,066	645	3,993
Rental Cars	<u>481</u>	<u>796</u>	<u>770</u>	<u>2,047</u>
	<u>\$15,502</u>	<u>\$16,306</u>	<u>\$12,877</u>	<u>\$44,685</u>

Although CHD's practice is to routinely send staff members to these conferences, we found that the agency had not established adequate controls (e.g., policies and procedures), relative to conference expenses. Consequently, we found potential problems with some of these expenses. For example, for each of the conferences, we found that CHD allowed as many as 13 employees, often from the same CHD program, to attend. We also found that some of the meal costs charged against state contracts during these conferences seemed excessive, including taxes and tips and the costs of meals for non-CHD employees.

Details of each of these conferences and a summary of our concerns follows:

Fiscal Year 1998: The International Association of Psychosocial Rehabilitation Services (IAPRS) Annual Conference, which was held in Orlando, Florida.

- Eleven CHD employees attended the conference: three employees who worked in CHD's Clubhouse program, six employees who worked in CHD's residential program, one employee who worked in CHD's Day Rehabilitation, and the Director of Psychosocial Rehabilitation Services. There was no documentation as to who was eligible to attend this conference or how the attendees were selected.
- On June 17, 1998, eight CHD employees and two guests went to the Crabhouse Restaurant in Orlando and purchased a meal for \$300, which was charged directly to various state contracts.
- On June 18, 1998, three CHD employees and two guests had a meal at Wolfgang Puck's that cost \$125, of which \$25 was reimbursed by the Director for that portion of the meal that was for her husband and son. The remaining \$100 expense was charged directly to a Residential and a Clubhouse Program.

Fiscal Year 1999: The IAPRS Annual Conference, which was held in Minneapolis, Minnesota.

- Thirteen CHD employees attended the conference: six employees who worked in CHD's Clubhouse Program, four employees who worked in CHD's residential program, two employees who worked in CHD's Day Rehabilitation, and the Director of Psychosocial Rehabilitation Services. There was no documentation as to who was eligible to attend this conference or how the attendees were selected.
- Two meals attended by CHD employees totaled \$1,066.43. These included a May 12, 1999 meal costing \$745.54 for CHD employees and three IAPRS presenters that included a \$100 tip and a May 11, 1999, meal for eight people that cost \$320.89.

Fiscal Year 2000: The IAPRS Annual Conference, which was held in Washington, D.C.

- Eleven CHD employees attended; four employees who worked in CHD's Clubhouse Program, three employees who worked in CHD's Residential Program, three employees who worked in CHD's Administrative Office, and the Director of Psychosocial Rehabilitation Services. There was no documentation as to who was eligible to attend this conference or how the attendees were selected.
- Various meal expenses included: on May 22, 2000, a meal attended by eight CHD employees cost \$428.90; on May 24 and 25, 2000, an employee charged crab cake dinners to his room costing \$80.96; and on May 25, 2000, a meal of \$135.72 was charged directly to a program that three people attended--CHD's Director of Programs, CHD's former Executive Director, and a CHD consultant.

Regarding this matter, CHD officials acknowledged that they could maintain better controls over the use of corporate credit cards and stated that the agency has developed written policies and procedures for the use of corporate credit cards that will comply with OSD guidelines relative to the documentation of expenditures.

Regarding attendance at conferences, on September 25, 2000, CHD officials provided a memorandum that detailed the process CHD officials said they used for selecting staff to attend these conferences. This memorandum stated, in part:

Discussion within the community on the focus of the conference, who seems to have an interest, the commitment and expectations from CHD from the people who will be attending. People need to be self-medicating, and independent. If flying is part of the conference, participants have to be willing to fly. A sign up sheet is posted. Members and staff that do not want to go volunteer to be part of the committee that interviews the people that want to go. The group designs a series of questions that they ask all the people that state they want to attend. The participants are rated as to how they answered the questions, involvement in the clubhouse, independence, residential staff are notified. Case managers are notified. Members and staff are then selected by this group to represent the clubhouse at the conference. Other staff members selected for training are randomly selected based on need.

Recommendation: In order to address our concerns relative to this matter, CHD's principal state purchasing agency (DMH), should recover from CHD the \$39,972 in undocumented, inadequately documented, and non-program-related expenses that it billed against its state contracts during our audit period. Also, DMH should conduct a review of the expenses for conferences CHD charged against its state contracts for the period during and subsequent to our audit period. Based on this review, DMH should recover whatever funds it deems appropriate. Finally, CHD should establish better controls over agency expenses. At a minimum, such controls should include requiring that the business nature of all expenses be adequately documented. In addition, CHD should independently review all expenses prior to payment to assess their reasonableness and allowability. Also, CHD should develop a formal written travel policy addressing the reimbursement of both local and out-of-state travel for all CHD employees and establish spending limitations for room, board, meals, and other travel-related expenses.

Auditee's Response: In response to this audit result, CHD officials provided the following comments:

...Some of the specific examples of expenses listed in the draft include a meal at Jae's in Boston for \$296.33 on the former Executive Director's account. This expense was for the meal served in conjunction with the first meeting of CHD's local Advisory Council. One CHD Board member, the Executive Director, the PSR Division Director, and the 5 new council members attended the meeting. The \$165.45 expense for Strip-T's and Buzz (a local Thai restaurant and deli) was for a meal for the staff who were in an all day strategic planning meeting at the main CHD office with 12 staff in attendance. The Internet expenses identified were for the Internet access at the corporate office of staff to communicate with the programs and were indeed for business purposes.

A major focus at CHD is providing psychosocial rehabilitation (PSR) services to individuals diagnosed with serious and persistent mental illness. . . . Additionally, CHD is very involved with the International Association of Psychosocial Rehabilitation Services (IAPSRS) the organization that provides training, advocacy and resources to organizations and individuals using or providing psychosocial rehabilitation services. CHD staff and consumers across the nine programs in the PSR division attend the conferences, as a part of our training curriculum, held yearly by both the ICCD and IAPSRS in order to assure we are on top of the latest models and information needed to provide high quality services to the consumers we serve. Staff take time away from their family obligations to attend these meetings which many times require them to travel on their weekend time. Many times staff will have worked a full day and then travel sometimes getting in late to the conference site as a result, from time to time it is necessary for an individual to eat their meals in their room. Typically, CHD gives staff and consumers a per diem to cover meal and transportation costs. Staff are very conscientious about keeping their receipts and keeping the total they spend within the per diem which has been set. The Department of Mental Health is completely aware of the fact that our staff and consumers attend these as well as many other necessary trainings. In fact, DMH staff have been attending these conferences so they too will be aware of the most current research and gain expertise in psychosocial rehabilitation services.

Auditor's Reply: In its response, CHD states the nature and purpose for some of the questionable agency expenses we identified during our audit. However, as stated in our report, the documentation provided to us by CHD relative to these expenses did not indicate their business purpose, and CHD should not have charged these expenses against its state contracts. Since CHD did not comment on the numerous other expenses we identified as being either undocumented, inadequately documented, or non-program related, we therefore assume that CHD concurs with our conclusion that these expenses should not have been charged against its state contracts.

As stated in our report, although CHD's practice is to routinely send staff to conferences, the agency has not established adequate controls over conference expenses. While we acknowledge the fact that attendance at conferences can be beneficial to an organization, it is important for organizations with limited resources such as CHD to ensure that costs associated with such conferences are reasonable and allowable. However, during our meetings with CHD staff and senior management, we were informed on a number of occasions that there was no formal travel policy in existence. There were no per diems in existence for meals or transportation costs, and no policy existed for travel, including hotels, airfare, or meals. While we understand that staff may have to travel both locally and out of state in order to better serve the programs that CHD operates, we feel that prudence and efficiency should be exercised when incurring program-related expenses and that a limited number of staff members should attend conferences in order to facilitate communication of programs, updates, and changes to other staff members. Lastly, as noted in our report, CHD officials stated that the Internet services in question were not for business purposes.

3. Inadequate Administrative Controls over \$440,599 in Consultant Services and \$14,039 in Questionable Consultant Costs

Our audit revealed that CHD lacked adequate administrative controls over its consultant services. Specifically, CHD did not have a process to document the need for goods and services, did not award all of its contracts using a competitive bidding process, did not always enter into formal written agreements with its consultants, lacked documentation of its consultants' qualifications (e.g., resumes), and approved various payments to consultants without adequate documentation to substantiate that the services billed were actually provided. We also found that one of the consultants that CHD utilized billed \$14,039 in questionable, excessive, and undocumented expenses. Some of these questionable costs included gifts for employees of the Department of Public Health (DPH) and a silk scarf as another gift. The specific problems we identified are discussed below.

Inadequate Controls over \$440,599 in Consultant Services: Sound business practices advocate that entities such as CHD establish and implement effective internal controls over their operations, including the administration of consultant contracts. Such controls not only serve to ensure that contract terms and conditions are met but also that contracting entities receive the highest-quality service at the lowest cost. Moreover, such controls serve to maintain the integrity of the contracting process and ensure that agency funds are safeguarded against loss, waste, or misuse. Additionally, the state's General Contract Conditions state: "Any subcontract entered into by the Contractor for the purposes of fulfilling the obligations under a Contract must be in writing . . . and shall be consistent with and subject to the provisions of these Commonwealth Terms and Conditions for Human and Social Services and a Contract."

We reviewed all the documentation being maintained by CHD relative to the \$440,599 in expenses for consultant services that it billed against its state contracts during our audit period. Our review revealed that CHD had not established adequate policies and procedures relative to its administration of consultant services. The specific problems we found are as follows:

- Contrary to sound business practices, CHD did not have a process to document the need for consultant services and did not procure these services using a competitive bidding process. As a result, CHD cannot be assured that all the services it purchased were necessary or that it received the highest quality of services at the lowest cost.
- CHD did not always enter into formal written agreements with its consultants. As a result, CHD lacked a mechanism to monitor each contractor's performance and to protect itself from any legal issues (e.g., claims made by either the contractor or CHD for nonperformance of work, liability claims for any property damage, or personal injury) that could arise. Total consultant costs paid without a contract totaled \$288,058 during the period of our review.
- CHD did not always maintain documentation of its consultants' qualifications (e.g., resumes, certifications, and licenses). In fact, of the six consultants files we reviewed, only one contained a resume. Without a process that verifies such qualifications, CHD cannot be assured that its consultants were qualified to provide the services for which they paid.

Questionable Consultant Expenses Totaling \$14,039: During our review of the documentation maintained by CHD relative to its expenses for consultant services, we found a number of problems

specific to one consultant. According to agency officials, this consultant was hired to perform the duties and responsibilities of the Massachusetts HIV Planning and Prevention Group (MPPG), Training Evaluation, and Needle Exchange Program under CHD's contract with the DPH. Specifically, her contract for the period July 1, 1997 to June 30, 1998 details her duties and responsibilities as follows:

- Provide all logistical support for a maximum of 12 MPPG and Leadership Council meetings annually.
- Provide administrative and logistical support for the activities of the MPPG Leadership Council and ad hoc subcommittees as needed.
- Provide administrative support related to program communications (e-mail, fax, etc.), produce camera-ready desktop publishing materials, and assist in heavy materials productions periodically.
- Submit bi-monthly reports to CHD listing the administrative and/or logistical support provided to (a) each meeting, (b) copies of the minutes of meetings, and (c) a summary description of materials produced for the MPPG and/or the Leadership Council and ad hoc subcommittees.

Our review of the documentation being maintained by CHD relative to the services provided by this consultant revealed at least \$14,039 in undocumented, inadequately documented, or non-program-related expenses paid by CHD to this consultant during our audit period, as indicated in the table below:

Center for Health and Development
Summary of Unallowable Consultant Expenses
Fiscal Years 1998 through 2000

Inadequately Documented	\$ 2,684
Undocumented	11,200
Non-Program Related	<u>155</u>
Total	<u>\$14,039</u>

The specific problems we found relative to this consultant's services are listed below:

- Although the consultant received \$161,364 for work done over a three-year period (July 1, 1997 to June 30, 2000), for fiscal years 1999 and 2000, during which the consultant received payments totaling \$131,323, CHD did not enter into a formal written contract with this individual. Therefore, it could not be determined whether services provided by this consultant and the compensation paid by CHD was appropriate.
- During our review, we noted documentation stating that the consultant purchased office furniture totaling \$119 for her home office through CHD. Although CHD was reimbursed for the cost of this purchase, the consultant inappropriately benefited from using CHD's tax-exempt status.

- The consultant purchased a gift on April 24, 1998 for an employee of DPH for \$68.55 and charged CHD for the cost of the gift. Also, on June 12, 1998, this consultant charged CHD \$46 for a wedding gift for a DPH employee. Since these expenses were not part of the consultant's contracted scope of services, CHD should not have paid these expenses.
- In February 1999, the consultant purchased a silk scarf costing \$40 and submitted the invoice to CHD, which the agency charged directly to a DPH AIDS prevention contract. Since this expense was not part of the consultant's contracted scope of services, CHD should not have paid this expense.
- During fiscal year 1998, this consultant was charging rental expenses for her computer and office space in her residence. The negotiated rate was \$130/month for rent and \$50/month for the computer rental. Beginning April 1998, the consultant began submitting invoices at a new rental rate of \$200/month for space and \$75/month for the computer. The consultant received \$2,565 in additional rental income over and above the agreed-upon rate during the period of our audit. However, there was no documentation indicating that CHD and the consultant had negotiated a new rate for these rental costs. CHD's Director of Administration and Finance requested an explanation from the consultant for the new rate and received the following explanation in a memorandum dated April 6, 1998 from the consultant, which stated: "Per your request, I am putting in writing an explanation for increased space and computer rental fees to be charged to the DPH contract. Due to increased contract dollars for increased contract services, and due to the resultant increased space requirements...I have increased space rental fees to be billed to the contract."
- On February 12, 1999, CHD paid this consultant \$1,200 for prepaid expenses. However, CHD did not have any supporting documentation to substantiate the nature of the expense or the services performed for this payment.
- On August 13, 1999, this consultant submitted an invoice for services in the amount of \$10,000, which CHD paid. However, no backup documentation was included to support this invoice. When the audit team requested supporting documentation relative to this consultant payment, we were provided with the following explanation in a memorandum dated June 8, 2000, stating: "The \$10,000 invoice...was for services provided as part of the Training Evaluation component of the contract. (The consultant), in accordance with her agreement with CHD, chose to contract with two psychologists to provide training evaluation services for specified DPH programs." Upon review of the two psychologists' contracts, it was noted that one of the psychologists was a former employee of CHD. According to the previously cited OSD regulations, expenses that are undocumented are nonreimbursable under state contracts.

CHD's Executive Director stated that in the future all consultants doing business with CHD will be required to enter into a formal written contract with the agency. Regarding the specific consultant discussed above, on June 8, 2000, CHD's Executive Director sent a memorandum to the audit team that stated, in part: "[the consultant] will conduct the administrative portion of her contract responsibilities from CHD offices and will not receive reimbursements for office space and computer use." In addition, in response to the \$10,000 payment without proper backup, this memorandum stated: "In the future, all

contract arrangements between [the consultant] and her organization's sub-contractors working on CHD projects will be fully disclosed prior to consultant engagement. A copy of these agreements will be on file at CHD central office." As for the purchasing of gifts by the consultant, CHD stated: "In the future, CHD will ensure that none of its employees, consultants or agents will be a part of any process to provide or financially administer the presentation of such tokens of appreciation that are questionable to the Office of the State Auditor." CHD officials also stated that they would be taking measures to improve agency controls over consultant services.

Recommendation: In order to address our concerns relative to this matter, DPH should recover from CHD the \$14,039 in undocumented and questionable consultant costs that the agency billed against its state contracts during the audit period. CHD should develop and implement specific administration policies and procedures relative to its administration of consultant services. In particular, these policies and procedures should require that all contracts over specific dollar amounts, to the extent possible, be awarded using a competitive bidding process. Contracts for these services should be executed and signed by all involved parties and should clearly delineate such terms and conditions as contract period, scope of services, compensation, and each party's warranties and liabilities. All contract awards and maximum obligations should be recorded in the minutes of CHD's board meetings, which should also document the need for all consultant services as well as each consultant's qualifications. CHD should not pay for any consultant expenses that are not authorized and are not allowable under state regulations.

Auditee's Response: In response to this audit result, CHD officials provided the following comments:

CHD has had a long-term working relationship with the consultants who provide services to our organization. In fact, [consultant's name] who is the consultant who worked with CHD on our DPH contracts has a system where any expense related to the MPPG contract is checked with and signed off on by the CHD Senior Manager in charge of her contract as well as DPH to assure the expenses and work provided were approved. As the DPH contracts are for technical assistance and logistics it was DPH's decision to tell CHD how they wanted their contract allocation utilized to meet the needs of the Massachusetts Planning and Prevention Group we worked on behalf. Therefore DPH authorized expenses for gifts purchased for long-time MPPG

members, who did not work for the Commonwealth, because of their extraordinary work done to benefit the group. A letter was given to the audit team from DPH explaining the nature of these expenses. Finally, the expense of \$10,000 to hire a former CHD employee as a consultant to complete the short-term work of DPH Training and Evaluation contract was necessary because of this individual's expertise and the need to complete this work in a relatively short period. Though [consultant's name] who held the contract with CHD to complete this process paid the consultant, she had a signed consultant agreement on site at CHD.

Auditor's Reply: As stated in our report, CHD lacked adequate administrative controls over its consultant contracts. Specifically, CHD does not have a process to document its need for consultant services, does not always enter into formal written agreements with its consultants, and does not always maintain documentation of its consultants' qualifications. The fact that CHD may have long-term working relationships with some of its consultants does not mitigate the need to have adequate controls over its contract administration activities. Without such controls, there is inadequate assurance that all of the expenses that CHD is charging against its state contracts for consultant services were actually incurred, and/or were reasonable, allowable, and allocable to state contracts. There was no provision in any of the consultant contracts that we reviewed that provided for these consultants to purchase gifts for DPH staff. If, as CHD contends in its response, DPH wanted to recognize the extraordinary work conducted by members of DPH's staff, the department should have purchased these gifts directly rather than using consultant contracts with its vendors to do so. Such a practice not only results in the misclassification and overstatement of consulting expenses but also creates a mechanism whereby state agencies could circumvent state procurement regulations.

Regarding the \$14,039 in undocumented and questionable consultant costs, although CHD attempted to explain the nature of these expenses, the agency could not provide us any documentation to substantiate that their explanations were in fact valid.

4. **Inadequate Controls over Personnel Files and Attendance Records and Undocumented Payroll Costs Totaling \$47,385**

We found that CHD was not maintaining all the information required by the General Contract Conditions and state regulations in its personnel files. Specifically, we examined the personnel files of

10 direct care staff and nine administrative staff members and found numerous instances in which these personnel files lacked all of the records required by the terms and conditions of CHD's state contracts. Additionally, we reviewed attendance records for two pay periods for 10 administrative staff members and determined that administrative employees at CHD do not submit attendance records as required by the AICPA and OSD's fiscal year 2000 UFR Audit and Preparation Manual. As a result, no documentation exists to substantiate the \$47,385 in compensation these 10 individuals received during this two-week period.

The 808 CMR 1.04(1), promulgated by OSD states, in part:

...personnel records shall be maintained for each employee in accordance with generally accepted accounting principles recommended by the AICPA and sufficient to meet the requirements of M.G.L. c.151, the Fair Labor Standards Act of 1938 and contract terms.

Also, according to the General Contract Conditions, service providers such as CHD are required to maintain detailed personnel records for all members of its staff. In addition, in the fiscal year 2000 UFR Audit and Preparation Manual, OSD requires the maintenance of employee attendance records for all employees of contracted service providers by stating:

Where employees perform duties that relate to more than one function, the salaries of such individuals, as well as all other expenses which pertain to more than one function, should be allocated to the separate functional categories, based on procedures that determine, as accurately as possible, the portion of the cost related to each function. In some cases, and particularly where most of an individual's time is spent on one function, estimates of the time spent on each function may be appropriate. However, in many cases the maintenance of employee time reports for all employees [required by OSD] will be practical and will result in a more accurate determination of the costs attributed to each function.

Finally, one of CHD's state purchasing agencies, the Department of Mental Retardation (DMR), under 115 CMR 7.06 has established requirements regarding provider staffing, including qualification levels; supervision standards; staff job descriptions; staff performance evaluations that should occur at least annually; training requirements, including relief staff, in areas of safety awareness, fire safety, first aid, and cardiopulmonary resuscitation; assurance that all professionals are licensed, certified, or registered, if required; and Criminal Offender Record Information (CORI) conducted by the provider for

all persons whose responsibilities may bring them into direct contact with individuals being supported and serviced.

However, our examination of the personnel records of 19 CHD employees (10 direct care and nine administrative) revealed that all of the personnel files reviewed lacked some of the records required by CHD's state contracts. Specifically, 14 lacked evidence of a CORI review and 18 folders had no evidence that the employee participated in any training. In addition, we reviewed the attendance records of 19 employees for the weeks ending June 30, 1999 and December 31, 1999 and found that the 10 administrative employees tested had no approved attendance records on file. During these two pay periods, these 10 employees were paid a total of \$47,385. CHD's policy states that exempt employees only have to submit attendance records on an exception basis. However, without such documentation, there is inadequate assurance that the level and quality of personnel services as agreed to by CHD are actually being provided in this program. In addition, when an exempt (administrative) employee works on more than one program during the week, there is no assurance that CHD is correctly allocating the costs of these employees to the appropriate program without approved attendance records indicating the amount of hours worked.

Recommendation: CHD should take measures to ensure that personnel files are maintained in accordance with state regulations and terms and conditions of its state contracts. In addition, CHD should require all employees to have a signed payroll record designating what programs were worked on during each pay period. Finally, DMH should conduct a review of the time and attendance records being maintained by CHD for its administrative staff for the past seven years. Based on this review, DMH should take whatever measures necessary to resolve this matter.

Auditee's Response: In response to this audit result, CHD officials provided the following comments:

We dispute the claim that CHD does not have all necessary personnel documents. We do agree however, that a cross-referencing system was not in place during the audit review period,

enabling ease of locating confidential personnel documents. CHD has implemented new filing guidelines for personnel files, which include cross-referencing of all documents not filed in the personnel folder as well as a checklist of required documents. Additionally, personnel files will be audited quarterly, to ensure compliance with State requirements. Finally, all CHD employees, exempt and non-exempt are now required to submit bi-weekly signed and approved timesheets.

Auditor's Reply: As stated in our report, we found numerous instances where CHD was not maintaining all the information in its personnel files required under its contracts. In its response, CHD contends that this information was missing as a result of a deficient cross-referencing system. However, to date the agency has not provided us with any of the personnel documents that were missing from the files we reviewed. Based on its response, CHD has taken measures to address this problem.

5. Inadequate Internal Controls over Furnishings and Equipment Totaling \$275,869

We found that CHD has not established adequate controls over its equipment items. Specifically, contrary to state regulations, CHD does not maintain an accurate inventory of its furnishings and equipment items. In addition, CHD could not provide documentation to adequately identify whether state or private funds were used to purchase items. As a result, there was inadequate assurance that CHD's furniture and equipment inventory, which as of June 30, 2000 had a reported value of \$275,869, was being properly safeguarded against loss, theft, or misuse.

OSD has established regulations that describe what contracted service providers, such as CHD, are required to do in order to properly safeguard their inventory of fixed assets. Specifically, 808 CMR 1.04(5) states, in part:

Any Contractor in possession of capital items, as defined in 808 CMR 1.02 shall label, maintain and keep on file a written inventory of the property in accordance with generally accepted accounting principles.

The American Institute of Certified Public Accountants (AICPA) Codification of Statements on Auditing Standards (SAS) defines an adequate internal control structure and what is required to properly safeguard the assets of the organization. Specifically, SAS No. 78 states:

Establishing and maintaining an internal control structure is an important management responsibility. In establishing specific internal control structure policies and procedures

concerning an entity's ability to record, process, summarize and report financial data that is consistent with management assertions embodied in the financial statements, some of the specific objectives management may wish to consider include the following:

Access to assets is permitted only in accordance with management's authorization.

The recorded accountability for assets is compared with the existing assets at reasonable intervals and appropriate action is taken with respect to any differences.

However, we found that, contrary to SAS and state requirements, CHD was not maintaining detailed records of its inventory that clearly list the description and location of each item, its historical cost or fair market value if donated, the date of purchase, or the source of acquisition of each asset (e.g., state, private, or donated). Finally, CHD did not have any policies and procedures in place to restrict access to these assets, did not perform annual physical counts of items such as furniture and equipment for comparison to inventory records, and did not affix identifying tags to all of its furniture and equipment items. Because of these deficiencies, there was inadequate assurance that CHD's inventory of furnishings and equipment, which as of June 30, 2000 had a reported value of \$275,869, was properly safeguarded against loss, theft, or misuse.

During our audit, we tested a sample of 66 items that appeared on CHD's inventory listing as of December 31, 2000. Although CHD provided us with an inventory listing with property tag numbers noted, during our test of these 66 items we found that 65 did not have a property tag or an identifying number affixed. In addition, CHD's inventory listing had 13 items that did not have any property tags assigned to the particular property. We also conducted site visits at two of CHD's program sites to conduct an inventory. During our visits to these two sites we found that none of the physical inventory located at these sites contained inventory tags. Also, we found three computers, a fax machine, a copier, a refrigerator, safes, printers, and televisions at these two program sites that were not listed on the agency's inventory listing, indicating that the agency's inventory records are inaccurate. CHD officials could not explain the inventory problems we found during our audit.

Recommendation: In order to ensure that its fixed assets are properly safeguarded, valued, and reported in its financial statements, CHD should establish controls over its inventory system that are in compliance with SAS requirements and the requirements of state regulations.

Auditee's Response: In response to this audit result, CHD officials provided the following comments:

CHD has conducted a widespread inventory and tagging process throughout the agency at least twice during the past ten years. CHD agrees we need to update the current list to develop a current inventory and to tag new equipment as well as to identify the source of funds used to purchase the items. CHD's Board set a limit of \$1,000 for equipment and \$2,000 for computer equipment during FY 2000.

Auditor's Reply: As stated in our report, CHD's fixed asset inventory system is deficient in numerous areas. Any inventory tagging process that CHD may have conducted did not address all of our concerns. However, based on its response CHD is taking measures to address our concerns relative to this matter.

6. Undisclosed Related-Party Transactions Totaling \$3,896

Our audit revealed that, contrary to state regulations, during fiscal year 1999 CHD did not accurately disclose a \$3,896 related-party transaction. This transaction involved the treasurer of CHD's Board of Directors, who is also the President and CEO of the vendor which CHD contracts with for its long distance telephone service. When we brought this matter to the attention of CHD officials, the agency sent a letter to their principal state-funding agency notifying it of the related-party transaction.

The 808 CMR 1.02 promulgated by OSD defines a related party as follows:

Any person or organization satisfying the criteria for a Related Party published by the Financial Accounting Standards Board in Statement of Financial Accounting Standards No. 57 (FASB 57).

FASB 57 states, in part:

Examples of related party transactions include transactions between (a) a parent company and its subsidiaries; (b) subsidiaries of a common parent; (c) an enterprise and trusts for the benefit of employees, such as pension and profit-sharing trusts that are managed by or under the trusteeship of the enterprise's management; (d) an enterprise and its principal owners, management, or members of their immediate families; and (e) affiliates. Transactions between related parties

commonly occur in the normal course of business. Some examples of common types of transactions with related parties are: sales, purchases, and transfers of realty and personal property, services received or furnished, for example, accounting, management, engineering, and legal services; use of property and equipment by lease or otherwise; borrowing and lendings, guarantees; maintenance of bank balances as compensating balances for the benefit of another; inter-company billings based on allocations of common costs; and filings of consolidated tax returns. Transactions between related parties are considered to be related party transactions even though they may not be given accounting recognition. For example, an enterprise may recover services from a related party without charge and not record receipt of the services.

In addition, 808 CMR 1.04(4) states:

Related Party Transactions: Notice of all Related Party transactions (including the relationship of the Related Party and a description of the nature and amount of the transaction) shall be made in writing to DPS and the Department(s) prior to their execution.

Beginning in September 1998, CHD's Board of Directors chose a vendor to process CHD's long distance telephone service. During fiscal years 1999 and 2000, CHD paid this vendor \$3,896 for long distance telephone services and billed these expenses against its state contracts. As the President and CEO of this vendor is also the Treasurer of CHD's Board of Directors, this transaction constituted a related-party transaction as defined by OSD regulations and should have been reported on CHD's fiscal years 1999 and 2000 UFRs. In addition, our review of CHD's board minutes revealed that no board member, including the Treasurer, abstained from voting on the long distance proposal, and no competitive proposals were obtained for this service to ensure that CHD was receiving the best service for the lowest possible price. When we brought this matter to the attention of CHD officials, they notified DMH in writing that these related-party transactions had occurred.

Recommendation: In order to address our concerns relative to this matter, CHD should take measures to ensure that all related-party transactions are disclosed in accordance with OSD regulations. Further, CHD should amend its fiscal year 1999 and 2000 UFRs to properly disclose the related-party transactions as previously noted that occurred during these two fiscal years.

Auditee's Response: In response to this audit result, CHD officials provided the following comments:

In earlier discussions with Audit Team, CHD has stated that we agree with this finding and have since corrected this to reflect a related party transaction and therefore accept this finding.

Auditor's Reply: We believe the action taken by CHD regarding this matter was necessary and appropriate. We recommend that in the future, all of CHD's related party transactions should be properly disclosed.