



# The Commonwealth of Massachusetts

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**INDEPENDENT STATE AUDITOR'S REPORT ON  
CERTAIN ACTIVITIES OF  
ALTERNATIVES UNLIMITED, INC.  
JULY 1, 2001 THROUGH JUNE 30, 2003**

**OFFICIAL AUDIT  
REPORT  
JANUARY 20, 2005**

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## TABLE OF CONTENTS/EXECUTIVE SUMMARY

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### INTRODUCTION

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1

Alternatives Unlimited, Inc. (AUI) was incorporated on August 28, 1974 as a private, nonprofit human services agency. AUI provides residential services, individual support, community support, training services, and transportation for developmentally and mentally disabled individuals who reside in the Blackstone Valley and surrounding areas.

The scope of our audit included the various administrative and operational activities of AUI during the period July 1, 2001 through June 30, 2003. Our audit was conducted in accordance with applicable generally accepted government auditing standards for performance audits issued by the Comptroller General of the United States and included audit procedures and tests that we considered necessary to meet those standards.

Our audit sought to determine whether AUI had implemented (1) effective internal controls, including processes for planning, organizing, directing and controlling program operations and (2) policies and procedures to ensure that resource use is consistent with laws and regulations and resources are safeguarded and efficiently used. We also sought to assess AUI's business practices and its compliance with applicable laws, rules, and regulations and the various fiscal and programmatic requirements of its state contracts.

Our audit found that the Department of Mental Health (DMH) used AUI as a fiscal conduit to pay for \$48,000 in undocumented and non-program expenses and for services provided to non-AUI clients, and was therefore in noncompliance with state law.

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### AUDIT RESULTS

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3

#### **DMH USED AUI AS A FISCAL CONDUIT TO PAY FOR \$48,000 IN INELIGIBLE EXPENSES**

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We found that contrary to Chapter 29, Section 29B, of the Massachusetts General Laws, DMH used AUI as a fiscal conduit to pay as much as \$48,000 of DMH and other expenses, including many that seemed unrelated to AUI's operations. AUI did not have adequate documentation to substantiate \$15,874 of these expenses; the remaining \$32,126, for which there was some documentation, did not seem related to AUI's program activities. For example, according to AUI officials, DMH instructed AUI to pay for \$7,003 in DMH expenses and \$25,123 for expenses incurred by other human services providers for non-AUI clients. By processing expenses in this manner, DMH failed to comply with state law and various regulations and inaccurately reported both its own and AUI's total operating expenses to the Commonwealth for the period of our review. As a result, DMH did not ensure that adequate controls were in place to protect these funds from abuse or misuse.

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### APPENDIX

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10

#### **AUI Programs**

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10

## INTRODUCTION

### *Background*

Alternatives Unlimited, Inc. (AUI) was incorporated on August 28, 1974 as a private, not-for-profit human services agency. AUI provides residential services, individual support, community support, training services, and transportation for developmentally and mentally disabled individuals who reside in the Blackstone Valley and surrounding areas. A description of the programs that AUI operated during our audit period appears in the Appendix.

AUI receives funding primarily from Commonwealth of Massachusetts contracts with the Department of Mental Retardation (DMR) and the Department of Mental Health (DMH). During our audit period, AUI received the following funding:

### Summary of Revenue July 1, 2001 through June 30, 2003

Revenue Source	Fiscal Year 2002	Fiscal Year 2003
Department of Mental Retardation	\$8,275,746	\$8,127,518
Department of Mental Health	6,187,205	6,418,807
Other State Agencies	485,790	482,022
Medicaid	2,061,685	2,061,492
Client Resources	668,195	690,537
Gifts, Contributions	343,894	311,954
Grants	20,000	40,000
Other	<u>142,159</u>	<u>392,681</u>
Total	<u>\$18,184,674</u>	<u>\$18,525,011</u>

### *Audit Scope, Objectives, and Methodology*

The scope of our audit included the various administrative and operational activities of AUI during the period July 1, 2001 through June 30, 2003. Our audit was conducted in accordance with applicable generally accepted government auditing standards for performance audits issued by the Comptroller General of the United States and included audit procedures and tests that we considered necessary to meet those standards.

Our audit objectives were to:

1. Determine whether AUI had implemented effective internal controls, including the following:
  - Processes for planning, organizing, directing, and controlling program operations
  - Policies and procedures to ensure that resource use is consistent with laws and regulations and resources are safeguarded and efficiently used
2. Assess AUI's business practices and its compliance with applicable laws, rules, and regulations and the various fiscal and programmatic requirements of its state contracts

To achieve our objectives, we first assessed the internal controls established and implemented by AUI 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 AUI's accounting system. We used this assessment in planning and performing our audit tests. We held discussions with AUI officials, reviewed the agency's Board of Director's meeting minutes for the audit period, and reviewed organizational charts, internal policies and procedures, and all applicable laws, rules, and regulations. We also examined AUI's financial statements, budgets, cost reports, invoices, and other pertinent financial records to determine whether expenses incurred under its state contracts were reasonable, allowable, allocable, properly authorized and recorded, and in compliance with applicable laws, rules, and regulations.

Our audit was limited to a review of the activities of AUI. Our audit was not conducted for the purposes of forming an opinion on AUI's financial statements. We also did not assess the quality and appropriateness of all program services provided by AUI under its state-funded contracts. Rather, our report is intended to report findings and conclusions on the extent of AUI's compliance with applicable laws, regulations, and contractual agreements and to identify services, processes, methods, and internal controls that could be made more efficient.

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## AUDIT RESULTS

### **DMH USED AUI AS A FISCAL CONDUIT TO PAY FOR \$48,000 IN INELIGIBLE EXPENSES**

We found that contrary to Chapter 29, Section 29B, of the Massachusetts General Laws, the Department of Mental Health (DMH) used AUI as a fiscal conduit to pay as much as \$48,000 in DMH and other expenses, including many that did not seem related to AUI's operations. For example, according to AUI officials, DMH instructed AUI to pay for \$7,003 in DMH expenses and \$25,123 for expenses incurred by other human services providers for non-AUI clients. By processing expenses in this manner, DMH failed to comply with state law and various regulations and inaccurately reported both its own and AUI's total operating expenses to the Commonwealth for the period of our review. Furthermore, DMH did not ensure that adequate controls were in place to protect these funds from abuse or misuse.

During fiscal year 1998, DMH entered into a seven-year cost-reimbursement contract with AUI to operate its Education and Employment Program in conjunction with Quinsigamond Community College (QCC); the annual maximum obligation of that contract was \$48,541. However, on May 24, 2002 the maximum obligation of this contract was amended, increasing nearly 100%, to \$96,541. We spoke with officials at QCC regarding this amendment. They stated that they neither initiated nor had any knowledge of the amendment and said they received only \$48,541 during fiscal year 2002—the original maximum obligation of this contract.

We reviewed AUI's fiscal year 2002 Uniform Financial Statements and Independent Auditor's Report (UFR) that it filed with the Commonwealth; the UFR showed that DMH reimbursed AUI \$96,541 for Education and Employment Program expenses. However, AUI's own financial records indicated that it incurred \$48,541 in costs for this program. We brought this matter to the attention of AUI's Fiscal Manager, who told us that during May 2002 DMH provided AUI with a list of various expenses to pay on behalf of DMH. These expenses were not associated with the Education and Employment Program. The Fiscal Manager stated that DMH officials instructed AUI to write checks to various stores, restaurants, movie theaters, and other vendors and charge these expenses against the contract that funded the Employment and Education Program. The Fiscal Manager stated that after checks were written, a DMH employee would pick them up at AUI's business office and deliver them to the respective vendors. We asked the Fiscal Manager whether DMH provided any invoices, bills, or other documentation to

AUI to substantiate these expenses. The Fiscal Manager informed us that, to her knowledge, the checks were being issued before the expenses were incurred by DMH, and that DMH did not provide any documentation regarding these expenses.

Based on the assertions of AUI's Fiscal Manager, during our audit we reviewed all the documentation that AUI and QCC were maintaining regarding these transactions and noted various problems:

**a. DMH Inappropriately Used AUI as a Fiscal Conduit**

Chapter 29, Section 29B, of the General Laws prohibits state agencies from using contracts with human services providers as fiscal conduits; it states, in part:

*Such contracts shall not be written or used by any department, office, agency, board, commission or institution of the commonwealth to procure full or part-time personal services, or equipment to be used by such department, office, agency, board, commission or institution, or any goods or services not required in the direct provision by the contractor of social, rehabilitative, health, or special education services to populations being served by the contracting department, office, agency, board, commission, or institution.*

We found that although DMH's contract with AUI for the Employment and Education Program was increased by \$48,000 to purportedly cover additional program expenses, those funds were not then used for that purpose. Rather, according to documentation we reviewed, DMH officials used AUI as a fiscal conduit and directed how the additional \$48,000 should be used. Of those funds, \$25,123 was used to pay six other human services providers for services to non-AUI clients; \$7,003 was used to pay for DMH expenses; \$10,474 was used to pay for AUI expenses not related to its Education and Employment Program; and the remaining \$5,400 was used by DMH to pay AUI an administrative fee for processing these \$48,000 in payments.

We asked a DMH official why AUI's contract was amended and contract funds were used in this manner. The official stated that these expenses were for "vouchers to buy items for the personal needs of DMH clients." The official added that some of these expenses may have gone to pay for expenses related to emergency situations. However, despite those assertions, neither DMH nor AUI provided any documentation to substantiate the rationale for paying the expenses in this manner.

**b. AUI and DMH Engaged in Questionable Billing Practices**

The Executive Office for Administration and Finance has promulgated 801 Code of Massachusetts Regulation (CMR) 21.08 (1), with which all state agencies must comply. This regulation states, in part:

*Contractor shall only be compensated for performance delivered to and accepted by the Department in accordance with the specific terms and conditions of a properly executed Contract.*

Moreover, according to Chapter 266, Section 67A, of the General Laws, it is a crime for a state agency to knowingly accept false invoices for supplies or services:

*Whoever, in any matter, relative to procurement of supplies, services or construction, as defined in section one of chapter twelve A, within the jurisdiction of any department, agency or public instrumentality of the commonwealth, or of any political subdivision thereof, intentionally:*

- (1) makes a material statement that is false;*
- (2) omits or conceals a material fact in a written statement;*
- (3) submits or invites reliance on a material writing or recording that is false, forged, altered, or otherwise lacking in authenticity;*
- (4) submits or invites reliance on a sample, specimen, map, photograph, boundary-mark, or other object that is misleading in a material respect; or*
- (5) uses any trick, scheme, or device that is misleading in a material respect;*

*shall be punished by a fine of not more than ten thousand dollars or by imprisonment in the state prison for not more than five years, or in the house of correction for not more than two and one-half years, or both.*

DMH instructed AUI to charge \$25,123 of expenses against its contracts for services provided to non-AUI clients by six other human services providers. Also, AUI charged \$7,003 in expenses for what was identified in AUI's records as "North County DMH." These payments appeared to be for unpaid bills, summer camps, supermarket expenses, and furniture for DMH—but not for AUI clients. Furthermore, \$10,474 was used to pay for AUI expenses not related to the Education and Employment Program. Since these program expenses were not used for their intended purposes as specified in the contract amendment and were improperly billed, they constitute unallowable program costs. Moreover, by using state funding in this manner, DMH was not only in noncompliance with state law and regulations—and inaccurately reported its own and AUI's operating expenses to the

Commonwealth for the period of our review—it also did not properly safeguard these funds against abuse and misuse. Finally, the \$5,400 in state funds that DMH paid to AUI as an administrative fee to process these payments constitute an unnecessary expense, because DMH’s internal accounting staff could have processed them.

**c. Expenses Were Undocumented**

According to regulations promulgated by the Office of the State Comptroller (OSC) with which all state agencies, such as DMH, must comply, state agencies must maintain adequate documentation for all expenses paid with state funds. Specifically, 815 CMR 10.00 states, in part:

*Departments shall maintain the Record Copy of the following documents in accordance with 815 CMR 10.00 and any policies and procedures issued by the Office of the Comptroller:*

- a. all bills and vouchers on which money has been paid or will be paid from the Treasury upon the certificate of the Comptroller or warrant of the Governor; and*
- b. all contracts under which money may be payable from the Treasury....*

*Departments shall maintain Record Copies of the documents identified under 815 CMR 10.03(1) at:*

- a. a central department location, or*
- b. if the department maintains record copies at multiple locations, the department shall maintain a centralized list of the repository location of all Record copies....*

Similarly, 808 CMR 1.05 (26) promulgated by the Operational Services Division (OSD) requires all contracted human services providers, such as AUI, to maintain adequate supporting documentation for all expenses and further identifies the following as being nonreimbursable expenses under state contracts:

*(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 reviewed the documentation that AUI was maintaining regarding the \$48,000 in expenses at issue and determined that none of the expenditures contained adequate documentation to substantiate that they had been incurred by AUI. In fact, for the



non-AUI expenses, the agency had only a spreadsheet provided to it by DMH officials indicating how the funds were used.

### ***Recommendation***

To address our concerns regarding this matter, DMH should discontinue using AUI and any other vendor agency as a fiscal conduit. DMH should not process any expenses in this unallowable manner and should take measures to ensure that it complies with state law and procurement regulations when purchasing goods and services. Furthermore, the Executive Office of Health and Human Services and the OSD should (1) review the expenses that DMH paid using funding it provided to AUI and (2) require DMH to take corrective measures necessary to address these issues.

### ***Auditee's Response***

In response to this issue, AUI provided comments, which are excerpted below:

*The Audit states "DMH Used AUI as a Fiscal Conduit to Pay for \$48,000 in Ineligible Expenses." This statement is a misrepresentation and would be more properly shown on an audit report of DMH. Alternatives does not dispute that the transaction you reference took place. We amended the contract at the request of a DMH official with the initial belief that the funds were to be used as part of the contract. Later, we were directed to disperse the funds for the legitimate needs of clients of several other agencies and Alternatives.*

*It is normal DMH practice to disperse funds each year to cover special client needs. Previously, this was done by amendments to individual contracts. DMH, in an attempt to more efficiently disperse the funds, initiated the transaction you are questioning. Alternatives was provided with a detailed spreadsheet by DMH with instructions for the disbursal of the funds. The spreadsheet contained details referencing who the funds were for, what would be purchased, and to whom to make the check payable. The checks were all payable to businesses for the purpose of purchasing items for DMH clients.*

*It is difficult to understand your statement "AUI did not have adequate documentation to substantiate \$15,874 of the expenses; the remaining \$32,126, for which there was some documentation, did not seem related to AUI's program activities. For example, according to AUI officials, DMH instructed AUI to pay for \$7003 in DMH expenses and \$25,123 for expenses incurred by other human services providers for non-AUI clients." The spreadsheet referenced above clearly states the client, agency and retail organization associated with every dollar involved.*

*Alternatives subsequently reported the entire transaction as required by the contract. Your report states "We reviewed AUI's fiscal year 2002 Uniform Financial Statements and Independent Auditor's Report (UFR) that it filed with the Commonwealth; the UFR showed that that DMH reimbursed AUI \$96,541 for Education and Employment Program expenses. However, AUI's own financial records indicated that it incurred \$48,541 in costs for this program." This is inaccurate.*

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*The 2002 UFR for this program clearly shows \$42,600 in expenses which reflect this transaction, less \$5,400, which is our standard administrative overhead amount.*

*. . . The report further misinterprets the documentation to arrive at the conclusion that "DMH was not only in noncompliance with state law and regulations --- and inaccurately reported its and AUI's operating expenses to the Commonwealth for the period of our review -- but also did not properly safeguard these funds against abuse and misuse." . . .*

***Auditor's Reply***

Contrary to what AUI states in its response, our report does not misrepresent the fact that DMH used AUI as a fiscal conduit to pay DMH's expenses. This issue was identified during our audit of AUI and it is therefore appropriate and necessary for us to disclose this issue in our report of the agency. While it may be a normal practice for DMH to disperse funds each year to cover special needs, it is DMH's responsibility to do so in a manner that is allowable and consistent with state law and regulations.

As stated in our report, we identified \$48,000 in ineligible expenses during our audit of AUI. AUI did not have adequate documentation to substantiate \$15,874 of these expenses; the remaining \$32,126, for which there was some documentation, did not seem related to AUI's program activities. For example, according to AUI officials, DMH instructed AUI to pay for \$7,003 in DMH expenses and \$25,123 for expenses incurred by other human services providers for non-AUI clients. By processing expenses in this manner, DMH failed to comply with state law and various regulations and inaccurately reported both its and AUI's total operating expenses to the Commonwealth for the period of our review. As a result, DMH also did not ensure that adequate controls were in place to protect these funds from abuse or misuse.

AUI did in fact have a spreadsheet that indicated the amounts paid to each vendor. However, contrary to what AUI contends, this spreadsheet does not represent adequate documentation of these expenses. Adequate documentation would include source documents such as invoices, receiving reports that document the date, nature, and amount of each expense.

Contrary to what AUI states in its response, our report is accurate relative to the costs incurred in its Education and Employment Program. AUI's fiscal year 2002 UFR does in fact indicate \$96,541 in expenses was incurred by AUI in its Education and Employment Program. However, our report correctly states that only \$48,541 in expenses were actually incurred in this

program. As AUI states in its response, the remaining \$48,000 was for non-program related expenses.

Contrary to what AUI asserts in its response, we did not misinterpret the documentation AUI provided to us relative to this matter. As stated in our report, DMH clearly used AUI as a fiscal conduit, a fact not disputed by AUI. In so doing, DMH failed to comply with state law and regulations and inaccurately reported both its own and AUI's total operating expenses to the Commonwealth for the period of our review. By using a conduit to pay expenses, DMH removed these funds from the controls afforded by the normal state contracting procedures and therefore DMH did not ensure that adequate controls were in place to protect these funds from abuse or misuse.

## APPENDIX

### AUI Programs

**Residential Services:** This program allows individual clients to be integrated into the community. Group homes, or “supervised living” options, allow consumers to maximize their independence and residential choices. The “shared living” program matches people with willing families or individuals in the community to create personalized living arrangements.

**Individual Supports:** This program provides consumers who are living in independent or semi-independent situations with intermittent or ongoing supports that are not part of a comprehensive set of residential and work day services; these supports assist consumers to achieve some measure of rights and dignity, individual control, community membership, relationships, personal growth and accomplishment, and personal well-being.

**Supported Employment:** This program provides for the evaluation of disabled individuals’ rehabilitation potential, the development of intensive on-the-job training and placement, and follow-up services, including observation and supervision at the training site and other services needed to support the individual in employment.

**Transportation Service:** This program provides consumers with transportation to and from programs and employment.