Audit Report

Macomb County
Community Mental Health Services Board

October 1, 2004 – September 30, 2005

Office of Audit
Central Regional Office
June 2010

JENNIFER M. GRANHOLM
GOVERNOR

STATE OF MICHIGAN
DEPARTMENT OF COMMUNITY HEALTH
OFFICE OF AUDIT
400 S. PINE; LANSING, MI 48933

JANET OLSZEWSKI
DIRECTOR

June 1, 2010

Mr. Louis Burdi, Chairperson
Macomb County Community Mental Health Services
22550 Hall Road
Clinton Township, Michigan 48036

Mr. John Kinch, Executive Director
Macomb County Community Mental Health Services
22550 Hall Road
Clinton Township, Michigan 48036

Ms. Janet Olszewski, Director
Department of Community Health
Capitol View Building – 7th Floor
Lansing, Michigan 48913

Dear Mr. Burdi, Mr. Kinch and Ms. Olszewski:

This is the final report from the Michigan Department of Community Health (MDCH) audit of Macomb County Community Mental Health Services for the period October 1, 2004 through September 30, 2005 and selected areas subsequent to September 30, 2005.

The final report contains the following: description of agency; funding methodology; purpose; objectives; scope and methodology; conclusions, findings and recommendations; financial status report; explanation of audit adjustments; contract reconciliation and cash settlement summary; and corrective action plans. The conclusions, findings, and recommendations are organized by audit objective. The corrective action plans include the agency's paraphrased response to the Preliminary Analysis and the Office of Audit's response to those comments where necessary.

If the agency disagrees with the MDCH audit findings, the agency must use the appeal process specified in Attachment 9.3.2.1 of the agency's contract with MDCH. The adjustments presented in this final report are an adverse action as defined by MAC R 400.3401. If disputing the adverse action, the agency must submit a request for the Medicaid Provider Reviews and Hearings Process pursuant to MCL 400.1 et seq. and MAC R 400.3401, et seq. within 30 days of the receipt of this letter. Requests must identify the specific audit adjustment(s) under dispute, explain the reason(s) for the disagreement, and state the dollar amount(s) involved, if any. The request must also include any substantive documentary evidence to support the position.

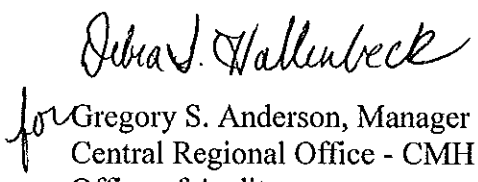
Requests must specifically identify whether the agency is seeking a preliminary conference, a bureau conference or an administrative hearing. If the agency does not appeal this adverse action within 30 days of receipt of this notice, this letter will constitute MDCH's Final Determination Notice according to MAC R 400.3405, and MDCH will implement the audit adjustments.

A request for the Medicaid Provider Reviews and Hearings Process must be sent within 30 days of receipt of this letter to:

Administrative Tribunal & Appeals Division
Michigan Department of Community Health
1033 S. Washington
P.O. Box 30763
Lansing, Michigan 48909

Thank you for the cooperation extended throughout this audit process.

Sincerely,



for Gregory S. Anderson, Manager
Central Regional Office - CMH
Office of Audit

GSA:wjb

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DESCRIPTION OF AGENCY

The Macomb County Community Mental Health Services Board (MCCMHSB) was established in October 1965, and operates under the provisions of the Mental Health Code, Sections 330.1001 – 330.2106 of the Michigan Compiled Laws.

The MCCMHSB provides outpatient, partial day, residential care, prevention, case management, MIChild, Adult Benefits Waiver (ABW), Children's Waiver and Omnibus Budget Reconciliation Act (OBRA) services to consumers within Macomb County.

MCCMHSB subcontracted with a number of independent agencies to provide services to its consumers. Macomb Oakland Regional Center, Inc. (MORC) was one of those agencies. The reimbursement arrangement between MCCMHSB and MORC consisted of a "net cost" payment methodology, which totaled approximately $42.3 million for FYE 2005.

The MCCMHSB administrative office is located in the city of Mount Clemens. The MCCMHSB board is comprised of 12 members who reside in Macomb County and are appointed for three-year terms.

FUNDING METHODOLOGY

MCCMHSB contracted with the Michigan Department of Community Health (MDCH) under a Managed Mental Health Supports and Services Contract (MMHSSC) for FYE 2005. This contract provided State General Funds (GF) for mental health and developmental disability supports and services to individuals with serious mental illness, serious emotional disturbances or developmental disabilities as described in Section 208 of the Mental Health Code. MCCMHSB received approximately $29.4 million of GF funding in FYE 2005. MCCMHSB also contracted with the MDCH under a Medicaid Managed Specialty Supports and Services Contract (MMSSSC). MDCH provided funding to MCCMHSB with both the state and federal share of Medicaid funds as capitated payments based on a Per Eligible Per Month (PEPM) payment methodology. MCCMHSB received approximately $99.7 million of Medicaid

Specialty Managed Care funding in FYE 2005. MCCMHSB also received special and/or designated funds, fee-for-service funds, MIChild capitated funds, and Adult Benefits Waiver (ABW) capitated funds under special contractual arrangements with MDCH. Each arrangement specifies the funding methodology. MIChild is a non-Medicaid program designed to provide certain medical and mental health services for uninsured children of Michigan working families. ABW provides health care benefits for Michigan's childless adult residents with incomes at or below 35% of the Federal Poverty Level.

PURPOSE AND OBJECTIVES

The purpose of the review was to assess the agency's performance relative to the requirements and best practice guidelines set forth in the contracts; to determine whether the agency properly reported revenues and expenditures in accordance with generally accepted accounting principles and contractual requirements; and to determine MDCH's share of costs in accordance with applicable requirements and agreements. Following are the specific objectives of this review:

Audit Objectives

1. To assess MCCMHSB's effectiveness and efficiency in establishing and implementing policies and procedures to ensure compliance with contractual and other legal requirements.
2. To assess MCCMHSB's effectiveness and efficiency in reporting their financial activity to MDCH in accordance with contractual requirements; applicable federal, state, and local statutory requirements; Medicaid regulations; and applicable accounting standards.
3. To determine MDCH's share of costs in accordance with applicable requirements and agreements, and to identify any balance due to or from MCCMHSB.

SCOPE AND METHODOLOGY

We examined MCCMHSB's records and activities for the period October 1, 2004 through September 30, 2005, as well as a limited review of certain subcontractor costs in FYE September 30, 2006. We reviewed and discussed the internal control questionnaire, completed by MCCMHSB's Finance Officer, to analyze the strength of the controls for the proper accounting of revenues and expenditures, procurement and other contracting procedures, reporting, claims management and risk financing. Discussions were held throughout the audit to update MCCMHSB's Finance Officer and other management personnel on the progress of the audit. MCCMHSB's policies and procedures were also reviewed. In addition, we performed comparable procedures at MORC, a major subcontractor for MCCMHSB. We summarized and analyzed revenue and expenditure account balances to determine if they were properly reported on the Financial Status Report (FSR) in compliance with the MMSSSC and the MMHSSC reporting requirements and applicable accounting standards. We performed our audit procedures from June 2006 through December 2006.

CONCLUSIONS, FINDINGS AND RECOMMENDATIONS

CONTRACT AND BEST PRACTICE GUIDELINES COMPLIANCE

Objective 1: To assess MCCMHSB's effectiveness and efficiency in establishing and implementing policies and procedures to ensure compliance with contractual and other legal requirements.

Conclusion: MCCMHSB was generally effective and efficient in establishing and implementing policies and procedures to ensure compliance with contractual and other legal requirements, except for the following: lack of segregation of duties in the accounts payable process (finding 1), inadequate review of subcontractor reported costs (finding 2), lack of internal control over the petty cash account (finding 3), lack of a capitalization policy (finding 4), improper accounting procedures for revenue (finding 5), and various financial reporting exceptions (findings 6 – 12).

Finding 1. Lack of Segregation of Duties in the Accounts Payable Process

MCCMHSB did not set up proper internal controls for the accounts payable process as required by the MMSSSC and the MMHSSC.

MCCMHSB employs an accounting clerk who utilizes the Integrated Financial Accounting System (IFAS) to process payments and process cash receipts. Good internal control practices do not allow receipts processing and payment processing to be done by the same individual. This situation does not provide for adequate segregation of duties.

MCCMHSB employs another accounting clerk who routinely generates purchase orders in IFAS, posts receiving reports in IFAS, processes payments in IFAS, and also mails checks to vendors. This also does not provide for adequate segregation of duties.

In these two instances, the inadequate segregation of duties compromised internal controls within the Accounts Payable Department. Internal controls should be strengthened to protect the CMH program integrity and the employees who administer the CMH program.

The MMSSSC, Part II, Section 6.6.1 states, in pertinent part, *"The PIHP shall maintain adequate internal control systems..."* and the MMHSSC, Part II, Section 6.6.1 states, in pertinent part, *"The CMHSP shall maintain adequate internal control systems…."*

Recommendation

We recommend that MCCMHSB adequately segregate duties related to the accounts payable process to strengthen internal controls as required by the MMSSSC and MMHSSC.

Finding 2. Inadequate Review of Subcontractor Reported Costs

MCCMHSB failed to adequately monitor subcontractor reported costs and detect unallowable costs charged to them by a subcontractor, which is in violation of the MMSSSC and the MMHSSC.

The MMSSSC, Part II, Section 6.4.2 Subcontracting, and the MMHSSC, Part II, Section 6.4.1 Provider Contracts, state, in pertinent part,

> *The PIHP/CMHSP may subcontract for the provision of any of the services specified in this contract…The PIHP/CMHSP shall be held solely and fully responsible to execute all provisions of this contract, whether or not said provisions are directly pursued by the PIHP/CMHSP, pursued by affiliated CMHSPs, or pursued by the PIHP/CMHSP through a subcontract vendor.*

Additionally, the MMSSSC, Part II, Section 6.6.1 states, in pertinent part, *"The PIHP shall maintain adequate internal control systems..."* and the MMHSSC, Part II, Section 6.6.1 states, in pertinent part, *"The CMHSP shall maintain adequate internal control systems…."*

MCCMHSB's review process of MORC's reported costs failed to detect unallowable bad debt expense. Additionally, MCCMHSB's review process failed to detect unallowable rental expenses from a contractual arrangement within the MORC structure. This resulted in MCCMHSB paying MORC for unallowable charges and reporting these costs to MDCH through the FSR.

Further details regarding the unallowable expenses and the financial impact are addressed in Findings 7 and 12.

Recommendation

We recommend that MCCMHSB strengthen their policies and procedures to more closely monitor subcontractor reported costs to ensure proper payments to subcontractors and the reporting of only allowable costs on the FSR as required by the MMSSSC and the MMHSSC.

Finding 3. Lack of Internal Control Over the Petty Cash Account

MCCMHSB did not set up proper internal controls for the petty cash account as required by the MMSSSC and the MMHSSC.

The petty cash account was reconciled by the same person that manages the account. This practice violates proper internal controls by creating a situation in which there is a lack of segregation of duties. A different staff member should be assigned to complete the reconciliation to ensure that the funds are properly managed and to decrease the risk of theft or fraud.

The MMSSSC, Part II, Section 6.6.1 states, in pertinent part, *"The PIHP shall maintain adequate internal control systems..."* and the MMHSSC, Part II, Section 6.6.1 states, in pertinent part, *"The CMHSP shall maintain adequate internal control systems…."*

Recommendation

We recommend that MCCMHSB establish proper internal controls for the petty cash account as required by the MMSSSC and the MMHSSC.

Finding 4. Lack of a Capitalization Policy

MCCMHSB did not have a written capitalization policy.

MCCMHSB must use the principles and standards of OMB Circular A-87 (relocated to 2 CFR Part 225) for determining all costs reported on the financial status report according to Section 6.6.1 of the MMSSSC and MMHSSC. Accordingly, MCCMHSB needs to establish a written capitalization policy to identify which of their property and equipment purchases are to be capitalized in compliance with 2 CFR Part 225.

According to 2 CFR Part 225, Appendix B, Section 15.b. (1) - (7), MCCMHSB is required to follow the rules for capital expenditures as listed below:

> *b. The following rules of allowability shall apply to equipment and other capital expenditures:*
>
> *(1) Capital expenditures for general purpose equipment, buildings, and land are unallowable as direct charges, except where approved in advance by the awarding agency.*
>
> *(2) Capital expenditures for special purpose equipment are allowable as direct costs, provided that items with a unit cost of $5,000 or more have the prior approval of the awarding agency.*

(3) Capital expenditures for improvements to land, buildings, or equipment which materially increase their value or useful life are unallowable as a direct cost except with the prior approval of the awarding agency.

(4) When approved as a direct charge pursuant to section 15.b (1), (2), and (3) of this appendix, capital expenditures will be charged in the period in which the expenditure is incurred, or as otherwise determined appropriate and negotiated with the awarding agency. In addition, Federal awarding agencies are authorized at their option to waive or delegate the prior approval requirement.

(5) Equipment and other capital expenditures are unallowable as indirect costs. However, see section 11, Depreciation and use allowance, for rules on the allowability of use allowances or depreciation on buildings, capital improvements, and equipment. Also, see section 37, Rental costs, concerning the allowability of rental costs for land, buildings, and equipment.

(6) The unamortized portion of any equipment written off as a result of a change in capitalization levels may be recovered by continuing to claim the otherwise allowable use allowances or depreciation on the equipment, or by amortizing the amount to be written off over a period of years negotiated with the cognizant agency.

(7) When replacing equipment purchased in whole or in part with Federal funds, the governmental unit may use the equipment to be replaced as a trade-in or sell the property and use the proceeds to offset the cost of the replacement property.

The lack of a capitalization policy could lead to inconsistent accounting treatment of capital asset purchases and violations of 2 CFR Part 225.

Recommendation

We recommend that MCCMHSB establish a written policy on Capitalization of Equipment and Fixed Assets that complies with 2 CFR Part 225.

Finding 5. Improper Accounting Procedures for Revenue

MCCMHSB did not record revenue on a timely basis, which is a violation of generally accepted accounting principles (GAAP), the MMSSSC and the MMHSSC.

The MMSSSC, Section 6.6.1, General, and the MMHSSC, Section 6.6.1, General, state, in pertinent part, *"The PIHP/CMHSP will comply with generally accepted accounting principles (GAAP) for governmental units when preparing financial statements."*

The MMSSSC, Attachment P 7.8.1, Section 1.3 Financial Status Report, and the MMHSSC, Attachment C 7.8.1, Section 1.3 Financial Status Report state, in pertinent part "…*With the exception of P.A. 423 Grant Funds, all reported revenue and expenditure information is required to be provided on an accrual basis of accounting. This accrual basis is expected to recognize all revenues and expenditures through the reporting periods….*"

According to GAAP:

- *Revenue recognition: Revenue is recognized when both of the following conditions are met:*
  - *a. Revenue is earned.*
  - *b. Revenue is realized or realizable.*
- *Revenue is earned when products are delivered or services are provided.*
  Realized means cash is received.
  Realizable means it is reasonable to expect that cash will be received in the future.

Model Waiver Revenues, totaling $765,931 for June through September, were not recorded until three to six months after earned and realizable in violation of generally accepted accounting principles (GAAP).

Recommendation

We recommend that MCCMHSB implement policies and procedures to record revenue on a timely basis as required by GAAP, the MMSSSC and the MMHSSC.

FINANCIAL REPORTING

Objective 2: To assess MCCMHSB's effectiveness and efficiency in reporting their financial activity to MDCH in accordance with contractual requirements; applicable federal, state, and local statutory requirements; Medicaid regulations; and applicable accounting standards.

Conclusion: MCCMHSB did not accurately report its financial activity to MDCH on the FYE 2005 FSR. We found exceptions in the following areas: lack of accrual for salary and wage expenditures (finding 6), unallowable bad debt expense (finding 7), expenditures exceeding authorizations improperly recorded (finding 8), internal service fund not reported or

supported (finding 9), improper accounting for unused funds (finding 10), differences between the FSR and the trial balance (finding 11), and unallowed rental expense (finding 12).

Finding 6. Lack of Accrual for Salary and Wage Expenditures

MCCMHSB failed to accrue salary and wage expenditures as required by the MMSSSC and the MMHSSC.

The MMSSSC, Attachment P 7.8.1, Section 1.3, Financial Status Report, and the MMHSSC, Attachment C 7.8.1, Section 1.3, Financial Status Report, state, in pertinent part, *"…all reported revenue and expenditure information is required to be provided on an accrual basis of accounting. This accrual basis is expected to recognize all revenues and expenditures through the reporting periods."*

MCCMHSB does not have a procedure in place to accrue salaries and wages at the end of each fiscal year. During FYE 2005, MCCMHSB reported payroll expenditures on the FSR that related to FYE 2004. MCCMHSB also recorded payroll expenditures on the general ledger in FYE 2006 that related to FYE 2005. By not recording accruals at the end of FYE 2004 and FYE 2005, some cost centers' payroll expenditures were either understated or overstated. The net impact to the FSR was an understatement of salary and wage expenditures of $39,928 for FYE 2005 and an overstatement in other periods. Adjustments were not made due to overall impact and immateriality.

Recommendation

We recommend that MCCMHSB implement policies and procedures to accrue salary and wage expenditures at the end of each fiscal year to ensure that expenditures are reported on the accrual basis of accounting as required by MMSSSC and MMHSSC.

Finding 7. Unallowable Bad Debt Expense

MCCMHSB paid a subcontractor for unallowable bad debt expense and included the expense on the FSR, which is in violation of the MMSSSC, MMHSSC, and federal cost principles.

MORC, a non-profit subcontractor, charged $45,518 to MCCMHSB under their cost reimbursement contract for bad debt expense related to the cost of care for developmentally disabled consumers. MCCMHSB paid MORC for this expense and reported the expense on the FSR to MDCH.

The Cost Principles for Non-Profit Organizations (OMB Circular A-122), located at 2 CFR, Part 230, must be used in determining the cost of work performed by non-profit organizations under cost reimbursement contracts in which costs are used in settlement according to Part 230.20(a). According to 2 CFR, Part 230.20(b), *"All cost reimbursement subawards (subgrants, subcontracts, etc.) are subject to those Federal cost principles applicable to the particular organization concerned. Thus, if a subaward is to a non-profit organization, this part shall apply…."*

Bad debts are an unallowable expense per 2 CFR, Part 230, Appendix B, Section 5. It states, *"Bad debts. Bad debts, including losses (whether actual or estimated) arising from uncollectible accounts and other claims, related collection costs, and related legal costs, are unallowable."* Therefore, under their cost reimbursement contract with MCCMHSB, MORC was not entitled to reimbursement for unallowable bad debt expense.

Furthermore, MCCMHSB's payment to MORC for unallowable bad debt expense is an unallowable expenditure on MCCMHSB's FSR to MDCH. MCCMHSB must use the principles and standards of OMB Circular A-87 (relocated to 2 CFR Part 225) for determining all costs reported on the financial status report according to Section 6.6.1 of the MMSSSC and MMHSSC. The payment of unallowable expenditures to a subcontractor is not reasonable and necessary, and, therefore, unallowable under 2 CFR Part 225. According to 2 CFR Part 225, Appendix A, Section C. Basic Guidelines, 1., *"Factors affecting allowability of costs. To be allowable under Federal awards, costs must meet the following general criteria: a. Be necessary and reasonable for proper and efficient performance and administration of Federal awards."*

Additionally, the Specialty Services Contract between MCCMHSB and MORC, Part VII, states, *"The AGENCY complies with all applicable local, state and federal laws governing the delivery of behavioral health services."* This requires the contracting party to comply with the federal regulations previously cited.

An adjustment to decrease the Medicaid expenses by $45,518 is shown on Schedules A.

Recommendation

We recommend that MCCMHSB implement policies and procedures to ensure that the FSR does not include unallowable bad debt expense, as required by federal cost principles and contractual agreements. We also recommend that MCCMHSB amend any subsequent FSRs to remove unallowable bad debt expense and re-settle those years with MDCH.

Finding 8. Expenditures Exceeding Authorizations Improperly Recorded

MCCMHSB recorded at least $11 million in expenditures to balance sheet accounts in their financial statements, and did not report these as expenditures on their FSRs in violation of contract provisions and GAAP over a several year period dating back to at least FYE 2000.

MCCMHSB's contracts with MDCH from FYE 1999 forward require that MCCMHSB report their TOTAL accrued expenditures on their FSRs, and comply with GAAP for financial reporting. However, MCCMHSB recorded expenditures that exceeded the MDCH authorization in balance sheet accounts instead of expense accounts from at least FYE 2000 through FYE 2005. These expenditures were not reported on the FSRs as required. Consequently, MDCH was not provided adequate expenditure information for monitoring, and MCCMHSB improperly reported amounts as receivables that were not receivables.

No financial adjustment is necessary because MCCMHSB used local funds to cover these costs.

Recommendation

We recommend that MCCMHSB implement policies and procedures to ensure total accrued expenditures are reported on FSRs, and compliance with GAAP for recording and reporting expenditures. Additionally, we recommend that MCCMHSB write off unsupported balance sheet account balances as prior period adjustments.

Finding 9. Internal Service Fund Not Reported or Supported

MCCMHSB established an Internal Service Fund (ISF) which was not properly supported nor disclosed to MDCH as required by 2 CFR Part 225, the MMSSSC and the MMHSSC.

MCCMHSB established an ISF in FYE 1998 with no determination of risk levels for the agency, and never reported it to MDCH. The ISF was established with funds from Macomb County. Neither Medicaid nor General Fund money was used to establish this risk reserve fund. Nevertheless, it should have been reported to MDCH as required by the MMSSSC and the MMHSSC. This lack of reporting impeded MDCH's ability to provide oversight over MCCMHSB's risk protections. Additionally, MCCMHSB never had a historical or actuarial study done to calculate the level of contributions into the fund as required by the MMSSSC and the MMHSSC.

The MMSSSC, Part II, Section 7.7.4, states, in pertinent part,

> *The PIHP must provide to MDCH upon request, documentation that demonstrates financial risk protections sufficient to cover the PIHP's determination of risk. The PIHP must update this documentation any time there is a change in the information. The PIHP may use one or a combination of measures to assure financial risk protection, including…creation of an ISF. The use of an ISF in this regard must adhere to Attachment P 7.7.4.1, and must be reported to the MDCH as required by the financial reporting requirements of this contract.*

The MMHSSC, Part II, Section 7.7.4, states in pertinent part,

> *The CMHSP must provide to the MDCH upon request, documentation that demonstrates financial risk protections sufficient to cover the CMHSP's determination of risk. The CMHSP must update this documentation any time there is a change in the information. The CMHSP may use one or a combination of measures to assure financial risk protection, including…creation of an ISF. The use of an ISF in this regard must adhere to Attachment C 7.7.4.1, and must be reported to the MDCH as required by the financial reporting requirements of this contract.*

The MMSSSC, Attachment P 7.7.4.1, Section M, and the MMHSSC, Attachment C 7.7.4.1, Section M, state, in pertinent part, *"Payments and funding levels of the ISF shall be analyzed and updated at least biannually pursuant to the provisions of OMB Circular A-87, Attachment B, paragraph 25 (d)(3)."*

OMB Circular A-87, Attachment B, paragraph 25.d.(3) [currently 2 CFR Part 225, Appendix B, Section 22.d.(3)], states, in pertinent part, *"Contributions to reserves must be based on sound actuarial principles using historical experience and reasonable assumptions. Reserve levels must be analyzed and updated at least biennially for each major risk being insured…."*

The MMSSSC, Part II, Section 7.8, states, in pertinent part, *"PIHPs that maintain an ISF Risk Reserve Account, and any form of reserve account are required to report on the status of these accounts on a quarterly basis, as well as year-end reports,"* and the MMHSSC, Part II, Section 7.8, states, in pertinent part, *"CMHSPs that maintain an ISF Risk Reserve Account, and any form of reserve account are required to report on the status of these accounts on a quarterly basis, as well as year-end reports."*

The MMSSSC, Section 6.6.1, General, states, in pertinent part, *"The PIHP shall maintain all pertinent financial and accounting records and evidence pertaining to this contract based on financial and statistical records that can be verified by qualified auditors,"* and the MMHSSC, Section 6.6.1, General, states, in pertinent part, *"The CMHSP shall maintain all pertinent financial and accounting records and evidence pertaining to this contract based on financial and statistical records that can be verified by qualified auditors."*

Recommendation

We recommend that MCCMHSB implement policies and procedures to report the ISF as required by the MMSSSC and the MMHSSC, and develop a historical computation or actuarial study to determine the appropriate funding balance for the ISF as required by the MMSSSC, MMHSSC, and 2 CFR Part 225.

Finding 10. Improper Accounting for Unused Funds

MCCMHSB improperly recorded unused funds from prior periods as a liability on their general ledger where no liability existed, which is in violation of the requirements of GAAP, the MMSSSC and the MMHSSC.

The MMSSSC, Section 6.6.1, General, states, in pertinent part, *"The PIHP will comply with generally accepted accounting principles (GAAP) for government units when preparing financial statements"* and the MMHSSC, Section 6.6.1, General, states in pertinent part, *"The CMHSP will comply with generally accepted accounting principles (GAAP) for governmental units when preparing financial statements."*

According to GAAP, the definition of a liability is: *"Liabilities --> probable future sacrifices of economic benefits arise from present obligations of an entity to transfer assets or provide services in the future as a result of past transactions or events."*

The MMHSSC, Section 7.2.9 – Adult Benefits Waiver (Section added with Amendment No. 1), states, *"FY 05 Adult Benefits Waiver funds unspent by 9-30-05 are local."*

The balance of $243,462 in the "Reserved – Managed Care Project" account represents unspent funds from prior fiscal periods, from programs such as the Adult Benefits Waiver. Since the $243,462 balance in the liability account "Reserved – Managed Care Project" represents unspent funds that become local according to the contract and they do not represent a liability, the funds should be transferred to MCCMHSB's equity fund balance.

Recommendation

We recommend that MCCMHSB implement policies and procedures to ensure all transactions are recorded in accordance with the requirements of GAAP, the MMSSSC and the MMHSSC. We also recommend that MCCMHSB write off this account balance as a prior period adjustment.

Finding 11. Differences Between the FSR and the Trial Balance

MCCMHSB did not report revenues and expenditures correctly on the FSR as compared to the amounts stated on the trial balance, which is in violation of the MMSSSC and MMHSSC.

Several line items on MCCMHSB's FSR did not agree with the trial balance. These line items affected both revenues and expenditures reported on the FSR.

Understatements in revenue were mainly due to unreported revenue and included: Grant Revenue of $213,851, Earned Contracts-Non-DCH Revenue (Substance Abuse) of $1,005, and Local Revenue of $999. The overstatement in revenue was due to a reporting error and included: Block Grant Revenue of $227.

Understatements in expenditures were mainly due to unreported expenses and included: Grant Expenses of $213,851, Earned Contracts-MDCH Expenditures of $1,005, Local Match of $999, and General Fund of $2,536. Overstatements in expenditures were due to reporting errors and included: Block Grant Expenses of $227 and Local Match of $2,499.

The MMSSSC, Attachment P 7.8.1, Section 2.3.1, Column C: Accrued YTD Actual and the MMHSSC, Attachment C 7.8.1, Section 2.3.1, Column C: Accrued YTD Actual state, in pertinent part, *"The amounts entered in this column are expected to represent year-to-date revenues received and/or accrued for the time period of the report. The amounts entered must include all earned reimbursements regardless of whether these have been billed or collected."*

The MMSSSC, Attachment P 7.8.1, Section 2.4.2, Column C: YTD Actual - Accrual Accounting Basis and the MMHSSC, Attachment C 7.8.1, Section 2.4.2, Column C: YTD Actual - Accrual Accounting Basis state, in pertinent part, *"The amounts entered in this column are expected to be on an accrual accounting basis for the time period of the report. This is to represent actual expenditures and expenditure obligations."*

Adjustments were made to the attached Schedule A (FSR). For revenues, increase Grant Revenue by $213,851, Earned Contracts-Non-DCH Revenue by $1,005, and Local Match Revenue by $999; and decrease Block Grant revenue by $227. For expenses, increase Grant Expenditures by $213,851, Earned Contracts-MDCH Expenditures by $778 [$1,005 + ($227)], and General Fund Expenditures by $2,536; and decrease Local Match Expenditures by $1,500 [($2,499) + $999].

Recommendation

We recommend that MCCMHSB implement policies and procedures to ensure that the revenues and expenditures reported on the FSR agree with the trial balance, as required by the MMSSSC and the MMHSSC.

Finding 12. Unallowable Rental Expense

MCCMHSB paid a subcontractor for unallowable rental expense and included the expense on the FYE 2006 FSR, which is in violation of the MMSSSC, MMHSSC, and federal cost principles.

MORC, a non-profit subcontractor, charged expenses to MCCMHSB in FYE 2006 under their cost reimbursement contract for rental expense related to the office building located at 16200 19 Mile Road in Clinton Township, Michigan. MCCMHSB paid MORC for this expense and reported the expense on the FSR to MDCH. However, the portion of this expense that exceeds underlying cost is unallowable.

The Cost Principles for Non-Profit Organizations (OMB Circular A-122), located at 2 CFR Part 230, must be used in determining the cost of work performed by non-profit organizations under cost reimbursement contracts in which costs are used in settlement according to Part 230.20(a).

According to 2 CFR, Part 230.20(b), *"All cost reimbursement subawards (subgrants, subcontracts, etc.) are subject to those Federal cost principles applicable to the particular organization concerned. Thus, if a subaward is to a non-profit organization, this part shall apply…."*

Rental costs under sale and lease back arrangements and rental costs under less-than-arms-length leases are allowable only up to the amount that would be allowed had the non-profit organization continued to own the property, or had title to the property vested in the non-profit organization according to 2 CFR, Part 230, Appendix B, Section 43. According to Section 43. c.,

> *…a less-than-arms-length lease is one under which one party to the lease agreement is able to control or substantially influence the actions of the other. Such leases include, but are not limited to those between divisions of a non-profit organization; non-profit organizations under common control through common officers, directors, or members;…For example a non-profit organization may establish a separate corporation for the sole purpose of owning property and leasing it back to the non-profit organization.*

MORC established MORC Holding Company on January 12, 2005, and, at the same time, created Metropolitan Real Estate Company, LLC (MREC). MORC Holding Company is the parent company for both MORC and MREC. MORC purchased the office building located at 16200 19 Mile Road, Clinton Township, MI, from the State of Michigan for $3,400,000 on September 28, 2005. On September 29, 2005, MORC sold the building to MREC for $1. A credit agreement of $3,400,000 between MORC, MREC and Fifth Third Bank was entered into on September 29, 2005, which obligated both MORC and MREC for the mortgage. On that same date, MORC also entered into a five-year lease agreement with MREC. The lease agreement obligated MORC to pay MREC the following annual lease payments:

Lease Year	**Annual Rent**
FYE 2006	$ 889,300
FYE 2007	$ 915,979
FYE 2008	$ 943,458
FYE 2009	$ 971,762
FYE 2010	$1,000,915

The rental costs MORC paid for the office building located at 16200 19 Mile Road were under a sale and lease back arrangement as defined by 2 CFR, Part 230, Appendix B, Section 43. Therefore, under MORC's cost reimbursement contract with MCCMHSB, MORC may only charge rental costs up to the amount that would be allowed had they continued to own the property. According to 2 CFR, Part 230, Appendix B, Section 43. b., this amount would include expenses such as depreciation or use allowance, maintenance, taxes, and insurance.

Had MORC continued to own the property, a total cost of $248,682 would be allowable in FYE 2006, which includes depreciation, interest, and a bank commitment fee. The other building costs (maintenance, taxes and insurance) are separate of the rental agreement and are allowable. The allowable depreciation expense for the 19 Mile Road building was calculated at $29,500 per year over a useful life of 20 years per the Estimated Useful Lives of Depreciable Hospital Assets, Revised 2004 Edition based on the purchase price of $3,400,000 less the land value of $2,810,000. MREC's general ledger and trial balance showed that the total interest paid to the mortgage company was $212,382. A commitment fee of $6,800 was paid to the bank when MORC and MREC took the loan. Since MORC paid $889,300 in rental expense for the 19 Mile Road office building, but only $248,682 was allowable, $640,618 of MORC's reported costs in FYE 2006 are unallowable. Of this amount, $171,350 was charged to MCCMHSB and $469,268 was charged to other counties.

MCCMHSB's payment to MORC for rental expense that exceeded the allowable amount ($171,350) is an unallowable expenditure on MCCMHSB's FYE 2006 FSR to MDCH. MCCMHSB must use the principles and standards of OMB Circular A-87 (relocated to 2 CFR Part 225) for determining all costs reported on the financial status report according to Section 6.6.1 of the MMSSSC and MMHSSC. The payment of unallowable expenditures to a subcontractor is not reasonable and necessary, and, therefore, unallowable under 2 CFR Part 225. According to 2 CFR Part 225, Appendix A, Section C. Basic Guidelines, 1., *"Factors affecting allowability of costs. To be allowable under Federal awards, costs must meet the following general criteria: a. Be necessary and reasonable for proper and efficient performance and administration of Federal awards."*

Additionally, in the Specialty Services Contract between MCCMHSB and MORC, Part VII Re-Contracting Requirements, Section B Corporate Compliance, Item 4 states, *"The AGENCY complies with all applicable local, state and federal laws governing the delivery of behavioral health services."* This requires the contracting party to comply with the federal regulations previously cited.

Recommendation

We recommend that MCCMHSB adopt policies and procedures to ensure that the FSR does not include expenses for unallowable rental costs, as required by federal cost principles and contractual agreements. We also recommend that MCCMHSB amend their FYE 2006 FSR and any other subsequent FSR's to remove unallowable rental costs and re-settle those years with MDCH.

MDCH'S SHARE OF COSTS AND BALANCE DUE MDCH

Objective 3: To determine MDCH's share of costs in accordance with applicable MDCH requirements and agreements, and to identify any balance due to or from MCCMHSB.

Conclusion: MDCH's obligations for FYE 2005 (excluding the MIChild capitated funds, MDCH Earned Contracts, Adult Benefits Waiver funds and Children's Waiver funds) after audit adjustments is $129,118,698. After considering advances and prior settlements there is no additional liability incurred by either MDCH or MCCMHSB.

MCCMHSB also needs to adjust the FYE 2006 and any subsequent settlements with MDCH that include unallowable bad debt expense and unallowable rental costs paid to MORC (addressed in Findings 7 and 12).

Macomb County Community Mental Health Services Board
Schedule A – Revenues
Adjusted Financial Status Report
October 1, 2004 through September 30, 2005

	REVENUES	Reported Amount	Finding 7	Finding 11	MCCMHSB	Total Adjustments	Adjusted Amount
A	Revenues Not Otherwise Reported	$58,228	$ -	$ -	$ -	$ -	$58,228
C	Earned Contracts - Non-MDCH Total	$ -	$ -	$1,005	$ -	$1,005	$1,005
1	CMH to CMH	-	-	-	-	-	-
2	Other	-	-	$1,005	-	$1,005	$1,005
3	Medicaid Managed Care	-					-
D	MI Child - Mental Health	$122,234	$ -	$ -	$ -	$ -	$122,234
D1	Adult Benefits Waiver	$2,109,236	$ -	$ -	$ -	$ -	$2,109,236
E	Local Funding Total	$6,153,503	$ -	$999	$ -	$999	$6,154,502
1	Special Fund Account (226(a))	-	-	-	-	-	-
2	Title XX Replacement	$52,937	-	$999	-	$999	$53,936
3	All Other	6,100,566	-	-	-	-	$6,100,566
4	Affiliate local Contribution to State Medicaid Match Provided from CMHSP	-	-	-	-	-	-
F	Reserve Balances Planned for Use	$449,504	$ -	$ -	$ -	$ -	$449,504
1	GF Carryforward - Sec 226(2)(b)(c)	$449,504	-	-	-	-	$449,504
2	Medicaid Savings	-	-	-	-	-	-
2a	Medicaid Savings - Substance Abuse	-	-	-	-	-	-
3	Internal Service Fund - Abatement	-	-	-	-	-	-
4	Internal Service Fund - Risk Corridor	-	-	-	-	-	-
5	Other (205(4)(h)) - Reserves - Vested Employee Benefit / Depreciation	-	-	-	-	-	-
6	Stop/Loss Ins	-	-	-	-	-	-

	REVENUES	Reported Amount	Finding 7	Finding 11	MCCMHSB	Total Adjustments	Adjusted Amount
G	DCH Earned Contracts Total	$4,542,878	$ -	$213,624	$ -	$213,624	$4,756,502
1	PASARR	378,588	-	-	-	-	378,588
2	Block Grants for CMH Services - Substance Abuse	3,902,621	-	(227)	-	(227)	3,902,394
3	DD Council Grants	-	-	-	-	-	-
4	PATH/Homeless	146,315	-	-	-	-	146,315
5	Prevention	-	-	-	-	-	-
6	Aging	-	-	-	-	-	-
7	HUD Shelter Plus Care	-	-	-	-	-	-
8	Other DCH Earned Contracts - SUBSTANCE ABUSE MI-CHILD	11,457	-	-	-	-	11,457
9	Other DCH Earned Contracts - SUBSTANCE ABUSE MI-ABW	103,897	-	-	-	-	103,897
10	Other MDCH Grants	-	-	$213,851	-	$213,851	213,851
H	GROSS MEDICAID TOTAL	$102,047,083	$ -	$ -	$(68,842)	$(68,842)	$101,978,241
1	Medicaid Specialty Managed Care	99,778,862	-	-	(68,842)	(68,842)	99,710,020
2	Medicaid - Childrens Waiver Total	2,268,221	-	-	-	-	2,268,221
I	REIMBURSEMENTS TOTAL	$847,608	$ -	$ -	$ -	$ -	$ 847,608
1	1st and 3rd Party	847,608	-	-	-	$ -	847,608
2	SSI	-	-	-	-	$ -	-
J	State General Funds Total	$29,408,678	$ -	$ -	$ -	$ -	$29,408,678
1	CMH Operations	23,051,090	-	-	-	-	23,051,090
2	Categorical Funding	371,032	-	-	-	-	371,032
3	State Services Base	5,986,556	-	-	-	-	5,986,556
K	Grand Total Revenues	$145,738,952	$	$215,628	$(68,842)	$146,786	$145,885,738
L	Estimated MDCH Obligation including Federal Medicaid	$133,687,231	$ -	$ -	$(68,842)	$(68,842)	$133,618,389

Macomb County Community Mental Health Services Board
Schedule A – Expenditures
Adjusted Financial Status Report
October 1, 2004 through September 30, 2005

	EXPENDITURES	Reported Amount	Finding 7	Finding 11	MCCMHSB	Total Adjustments	Adjusted Amount
A	Gross Total Expenditures	$145,581,135	$(45,518)	$215,665	$(13,022)	$157,125	$145,738,260
B	Expenditures Not Otherwise Reported	$58,228	$ -	$ -	$ -	-	$58,228
D	Earned Contracts (Non MDCH) Total	$ -	$ -	$ -	$ -	$ -	$ -
1	CMH to CMH	-	-	-	-	-	-
2	Other Earned Contracts	-	-	-	-	-	-
3	Medicaid Managed Care - Affiliate	-	-	-	-	-	-
F.	Local Total	$4,694,368	$ -	$(1,500)	$	$(1,500)	$4,692,868
1	Local Cost for State Provided Services	614,465	-	-	-	-	614,465
2	Other Not Used as Local Match	2,289,622	-	(1,603)		(1,603)	2,288,019
3	Affiliate Local Contribution to State Medicaid Match Provided to PIHP	-	-	-	-	-	-
4	PIHP Contribution to State Medicaid Match Provided to MDCH	1,790,281	-	103		103	1,790,384
5	Prior Year Carry-Forward	-	-	-	-	-	$ -
G	Expenditures From Reserve Balances	$449,504	$ -	$ -	$ -	$ -	$449,504
1	Carryforward - Sec 226(2)(b)(c)	449,504	-	-	-	-	449,504
2	Medicaid Savings	-	-	-	-	-	-
2.a	Medicaid Savings - Substance Abuse	-	-	-	-	-	-
3	Internal Service Fund - Abatement	-	-	-	-	-	-
4	Other (205(4)(h)) - Reserves - Vested Employee Benefits/Depreciation	-	-	-	-	-	-
5	Stop/Loss Ins.	-	-	-	-	-	-

	EXPENDITURES	Reported Amount	Finding 7	Finding 11	MCCMHSB	Total Adjustments	Adjusted Amount
H	MDCH Earned Contracts Total	$4,536,477	$ -	$214,629	$	$214,629	$4,751,106
1	PASARR	378,588	-		-		378,588
2	Block Grant for CMH Services	3,902,621	-	778		778	3,903,399
3	DD Council Grants	-	-	-	-	-	-
4	PATH/Homeless	146,315	-	-	-	-	146,315
5	Prevention	-	-	-	-	-	-
6	Aging	-	-	-	-	-	-
7	HUD Shelter Plus Care	-	-	-	-	-	-
8	Other MDCH Earned Contracts - Substance Abuse MI Child	5,056	-	-	-	-	5,056
9	Other MDCH Earned Contracts - Substance Abuse ABW	103,897	-	-	-	-	103,897
10	Other MDCH Grants	-	-	213,851	-	213,851	213,851
I	Matchable Services (A-(B through H))	$135,842,558	$(45,518)	$2,536	$(13,022)	$(56,004)	$135,786,554
J	Payments to MDCH for State Services	$5,662,696	$ -	$ -	$(13,022)	$(13,022)	$5,649,674
K	Specialty Managed Care Service Total	$104,244,077	$(45,518)	$ -	$ -	$(45,518)	$104,198,559
1	100% MDCH Matchable Services	103,199,973	(45,518)	-	-	(45,518)	103,154,455
2	All SSI and Other Reimbursements	-	-	-	-	-	-
3	Net MDCH Share for 100 % Services (K1-K2)	103,199,973	(45,518)	-	-	(45,518)	103,154,455
4	QAAP Expenditures	1,044,104	-	-	-	-	1,044,104
5	Total MDCH (K3+K4)	104,244,077	(45,518)	-	-	(45,518)	104,198,559

	EXPENDITURES	Reported Amount	Finding 7	Finding 11	MCCMHSB	Total Adjustments	Adjusted Amount
L	GF Categorical and Formula Services Total	$21,496,439	$ -	$2,536	$ -	$2,536	$21,498,975
1	100% MDCH Matchable Services	6,057,478	-	(9,541)	-	(9,541)	6,047,937
2	All SSI and Other Reimbursements	-	-	-	-	-	-
3	Net GF and Formula for 100% Services (L1-L2)	6,057,478	-	(9,541)	-	(9,541)	6,047,937
4	90/10 Matchable Services	15,438,961	-	12,077	-	12,077	15,451,038
5	Reimbursements	847,608	-	-	-	-	847,608
6	10% Local Match Funds	1,459,135	-	1,208	-	1,208	1,460,343
7	Net GF and Formula for 90/10 Services (L4-L5-L6)	13,132,218	-	10,869	-	10,869	13,143,087
8	Total MDCH GF and Formula (L3+L7)	19,189,696	-	1,328	-	1,328	19,191,024
L a	MI Child Mental Health	$213,305	$ -	$ -	$ -	$	$213,305
1	MI Child Mental Health - Capitation - Medicaid Only	122,234	-	-	-	-	122,234
2	MI Child Mental Health - MDCH GF Operations Base	91,071	-	-	-		91,071
L b	Adult Benefits Waiver	$1,957,820	$ -	$ -	$ -	$	$1,957,820
1	ABW - Capitation - Medicaid and State Match	1,957,820	-	-	-		1,957,820
2	ABW - MDCH GF Operation Base	-	-	-	-	-	-
M	Children's Waiver - Total	$2,268,221	$ -	$ -	$ -	$	$2,268,221
1	Medicaid	2,268,221	-	-	-		2,268,221
2	Other Reimbursements	-	-	-	-	-	-
3	MDCH GF Operations Base	-	-	-	-	-	-
N	Unobligated Spending Authority Total	$ -	$ -	$ -	$ -	$ -	$ -
1	DCH Risk Authorization	-	-	-	-	-	$ -
2	All Other	-	-	-	-	-	$ -
O	Total Local Funds (F+L6)	$6,153,503	$ -	$1,208	$ -	$1,208	$6,154,711
P	Total MDCH Share (J+K5+L8+La+Lb+M1+M3)	$133,535,815	$(45,518)	$1,328	$(13,022)	$(57,212)	$133,478,603

Finding 7: To disallow bad debts expense
Finding 11: To adjust the line items in the FSR to match the Trial Balance
MCCMHSB: To record MDCH's cost settlement adjustments made subsequently by MCCMHSB

Macomb County Community Mental Health Services Board

Schedule B

Contract Reconciliation and Cash Settlement Summary

October 1, 2004 through September 30, 2005

		MDCH Revenue	MDCH Expense
I.	Specialized Managed Care (Includes State and Federal Share)		
A	Total - Specialized Managed Care	$99,710,020	$104,198,559
B	Maintenance of Effort – Summary	$ -	$ -
C	Net Specialized Managed Care (A-B)	$99,710,020	$104,198,559

II.	State/General Fund Formula Funding		
A	GF/Formula - State and Community Managed Programs	Authorization	MDCH Expense
1	State Managed Services	$5,986,556	$5,649,674
2	MDCH Risk Authorization - MDCH Approved for Use	$ -	$ -
3	Community Managed Services	$23,422,122	$19,282,095
4	Total State and Community Programs - GF/Formula Funding	$29,408,678	$24,931,769
B	Maintenance of Effort – Summary	$ -	$ -
C	Categorical, Special and Designated Funds		
1	Categorical	$371,032	$371,032
2	Special Funds	$ -	$ -
3	Total Categorical, Special and Designated Funds	$371,032	$371,032
D	Subtotal-GF/Formula Community and State Managed Programs	$29,037,646	$24,560,737

		Specialized Managed Care	Formula Funds
III.	Shared Risk Arrangement		
A	Operating Budget – Exclude MOE and Categorical Funding	$99,710,020	$29,037,646
B	MDCH Share - Exclude MOE and Categorical Funding	$104,198,559	$24,560,737
C	Surplus (Deficit)	$(4,488,539)	$4,476,909
D	Redirect Formula Funds to Medicaid Recipients	$4,476,909	$(4,476,909)
E	Shared Risk - Surplus (Deficit)	$(11,630)	$ -
F	Risk Band – 5% of Operating Budget (A*5%)	$4,985,501	$1,451,882

Macomb County Community Mental Health Services Board

Schedule B

Contract Reconciliation and Cash Settlement Summary

October 1, 2004 through September 30, 2005

IV.	Cash Settlement	MDCH Share	Re-Direct		Total	Grand Total
A	MDCH Obligation					
1	Specialty Managed Care (Net of MOE)	$99,710,020	$ -		$99,710,020	
2	GF/Formula Funding (Net of Categorical and MOE)	$24,560,737	$4,476,909		$29,037,646	
3	MOE Specialty Managed Care MDCH Obligation	$ -	$ -		$ -	
4	MOE GF/Formula Funding MDCH Obligation	$ -	$ -		$ -	
5	Categorical - MDCH Obligation	$371,032	$ -		$371,032	
6	Total - MDCH Obligation					$129,118,698
B	Advances – Prepayments					
1	Specialized Managed Care - Prepayments Through 9/30/2005			$98,340,944		
2	Specialized Managed Care - FY 05 Prepayments Received After 9/30/2005			$1,369,076		
3	Subtotal - Specialized Managed Care				$99,710,020	
4	GF/Formula Funding - (Include MDCH Risk Authorization)				$23,051,090	
5	Purchase of Services				$5,986,556	
6	Categorical Funding				$371,032	
7	Total Prepayments					$129,118,698
C	Balance Due CMH/(MDCH)					$ 0
D	Balance Due to MDCH for Unpaid State Service Costs					
	State Facility Costs				$5,649,674	
	Actual Payments to MDCH				$5,649,674	
	Balance Due MDCH/(CMH)					$ 0
E	Net Balance Due MDCH					$ 0
	Prior Settlements					$ 0
F	Balance Due to MDCH (CMH)					$ 0

Corrective Action Plan

Finding Number: 1

Page Reference: 4

Finding: **Lack of Segregation of Duties in the Accounts Payable Process**

MCCMHSB did not set up proper internal controls for the accounts payable process as required by the MMSSSC and the MMHSSC.

Recommendation: Segregate duties related to the accounts payable process to strengthen internal controls as required by the MMSSSC and MMHSSC.

Comments: The MCCMH Finance Department routinely reviews and monitors all finance staff assignments in the interest of ensuring that there is appropriate segregation of duties.

Corrective Action: Staff duties for the two positions indicated have already been revised so that Account Clerk staff who receive funds do not also process payments. In addition, the purchasing function has been modified, with one Account Clerk generating purchase orders, and another processing the payments and mailing the checks to vendors.

Anticipated Completion Date: Completed.

MDCH Response: None.

Corrective Action Plan

Finding Number: 2

Page Reference: 4

Finding: **Inadequate Review of Subcontractor Reported Costs**

MCCMHSB failed to adequately monitor subcontractor reported costs and detect unallowable costs charged to them by a subcontractor, which is in violation of the MMSSSC and the MMHSSC.

Recommendation: Strengthen policies and procedures to more closely monitor subcontractor reported costs to ensure proper payments to subcontractors and the reporting of only allowable costs on the FSR as required by the MMSSSC and the MMHSSC.

Comments: MCCMH Finance Staff review expense reports on a monthly basis to identify expenditures that are unallowable to the Board. MCCMH meets with subcontractors on a regular basis and provides training on allowable expenditures and allowable services. MCCMH also conducts internal audits to review expense reports, and conducts Medicaid Verification Audits annually to ensure that appropriate services are reimbursed. In this one instance, the bad debt expense was charged after both the 1st and 2nd close reports from the subcontractor. It was reported on their 3rd close report, and was undetected.

Corrective Action: MCCMH will continue to monitor expense reports, continue to meet on a regular basis with providers, and continue to conduct training for providers to ensure that they fully understand what type of expenditures/services are allowable. MCCMH will ensure that all expense reports at year end are carefully reviewed for last minute changes.

MCCMH has been conducting internal audits of select providers. MCCMH will expand the internal audit process for all net cost providers to ensure that the expenditures which they submit to MCCMH are allowable. In addition, MCCMH plans on having the compliance auditors that audit the Board through the MDCH Compliance Audit do an on-site review of the largest provider, Macomb Oakland Regional Center.

Anticipated Completion Date: MCCMH is currently monitoring subcontractors in a number of ways. MCCMH will look at adding Macomb Oakland Regional Center as a separate review during the MDCH Compliance Audit beginning with the current fiscal year.

MDCH Response: None.

Corrective Action Plan

Finding Number: 3

Page Reference: 5

Finding: **Lack of Internal Control Within the Petty Cash Account**

MCCMHSB did not set up proper internal controls for the petty cash account as required by the MMSSSC and the MMHSSC.

Recommendation: Implement policies and procedures to establish proper internal controls for the petty cash account as required by the MMSSSC and the MMHSSC.

Comments: MCCMH recognizes the importance of separating duties in ensuring control over the Petty Cash account.

Corrective Action: The process for managing the Petty Cash account was revised in that there are two separate Account Clerks that have interaction with the Petty Cash Account. One Account Clerk pays funds out of Petty Cash, and a separate Account Clerk reconciles the fund and requests replenishment. The Board will also implement a separate policy and detail procedures that deals specifically with the handling of Petty Cash.

Anticipated Completion Date: This correction has already been addressed and changes made in terms of staff. A separate policy will be developed by August 2010.

MDCH Response: None.

Corrective Action Plan

Finding Number: 4

Page Reference: 6

Finding: **Lack of a Capitalization Policy**

MCCMHSB did not have a written capitalization policy.

Recommendation: Establish a written policy on Capitalization of Equipment and Fixed Assets that complies with 2 CFR Part 225.

Comments: MCCMH Finance understands the importance of a capitalization policy on equipment and fixed asset purchases to ensure consistent accounting treatment of capital asset purchases.

Corrective Action: MCCMH has already developed a Capitalization Policy which describes the standards for capital asset purchases.

Anticipated Completion Date: Completed.

MDCH Response: None.

Corrective Action Plan

Finding Number: 5

Page Reference: 8

Finding: **Improper Accounting Procedures for Revenue**

MCCMHSB did not record revenue on a timely basis, which is in violation of GAAP, the MMSSSC and the MMHSSC.

Recommendation: Implement policies and procedures to record revenue on a timely basis as required by GAAP, the MMSSSC and the MMHSSC.

Comments: MCCMH Finance recognizes that all revenues are to be accounted for on the accrual basis of accounting with the exception of PA 423 Grant Funds. MCCMH established accrual numbers to ensure that the revenue is recorded in the proper fiscal year. In this instance, the revenue item was not accrued on a timely basis.

Corrective Action: MCCMH will establish written policies and procedures to record the process by which revenues are to be recorded and accruals established to ensure that revenues are properly recorded in the correct accounting period.

Anticipated Completion Date: August 2010.

MDCH Response: None.

Corrective Action Plan

Finding Number: 6

Page Reference: 9

Finding: **Lack of Accrual for Salary and Wage Expenditures**

MCCMHSB failed to accrue salary and wage expenditures as required by the MMSSSC and the MMHSSC.

Recommendation: Implement policies and procedures to accrue salary and wage expenditures at the end of each fiscal year to ensure that expenditures are reported on the accrual basis of accounting as required by MMSSSC and MMHSSC.

Comments: MCCMH Finance recognizes that all expenditures must be reported on the accrual basis. MCCMH establishes accruals to ensure that expenditures are recognized in the appropriate accounting period.

Corrective Action: There is already a procedure in place to ensure that payroll expenditures are recorded in the proper period. If a pay period crosses two fiscal years, journal entries are made to ensure that the number of days falling into each year are correctly identified. Both payroll and related fringe benefit expenditures are adjusted.

Anticipated Completion Date: Completed.

MDCH Response: None.

Corrective Action Plan

Finding Number: 7

Page Reference: 10

Finding: **Unallowable Bad Debt Expense**

MCCMHSB paid a subcontractor for unallowable bad debt expense and included the expense on the FSR, which is in violation of the MMSSSC, MMHSSC, and federal cost principles.

Recommendation: Implement policies and procedures to ensure that the FSR does not include unallowable bad debt expense. Amend subsequent FSRs to remove unallowable bad debt expense and re-settle those years with MDCH.

Comments: MCCMH Finance recognizes that bad debt expense is an unallowed expense. As indicated in Finding Number 2, MCCMH continues to work with sub-contractors in monitoring the expenditures that the sub-contractors charge to MCCMH to ensure that the sub-contractors are not billing for expenditures which are unallowable. In addition, MCCMH closely monitors sub-contractor expenditure billings on a monthly basis to detect possible unallowable expenditures. MCCMH will ensure that subsequent year end reports are reviewed for possible changes.

Corrective Action: As indicated in Finding Number 2, MCCMH will expand the internal audit process for all net cost contracts. Macomb Oakland Regional Center will be subject to a separate review during the MCCMH CMH Compliance Audit.

Anticipated Completion Date: The intended review of Macomb Oakland Regional Center by the CMH Compliance auditors will begin with the current fiscal year.

MDCH Response: None.

Corrective Action Plan

Finding Number: 8

Page Reference: 11

Finding: **Expenditures Exceeding Authorizations Improperly Recorded**

MCCMHSB recorded at least $11 million in expenditures to balance sheet accounts in their financial statements, and did not report these as expenditures on their FSRs in violation of contract provisions and GAAP over a several year period dating back to at least FYE 2000.

Recommendation: Implement policies and procedures to ensure total accrued expenditures are reported on FSRs, and compliance with GAAP for recording and reporting expenditures. Additionally, write off unsupported balance sheet account balances as prior period adjustments.

Comments: Current MCCMH finance staff has worked extensively to ensure that total accrued expenditures are reflected on the FSR and that balance sheet accounts are not used to record expenditures.

Corrective Action: These corrections have already been addressed and changes made. MCCMH worked collaboratively with the Macomb County Finance Department to put a plan in place to resolve this issue. MCCMH will establish written policies and procedures to ensure that the FSR includes all expenditures and that MCCMH is in compliance with GAAP for reporting expenditures. MCCMH has worked to ensure that unsupported balance sheet accounts are written off appropriately.

Anticipated Completion Date: August 2010.

MDCH Response: None.

Corrective Action Plan

Finding Number: 9

Page Reference: 12

Finding: **Internal Service Fund Not Reported or Supported**

MCCMHSB established an Internal Service Fund (ISF) which was not properly supported nor disclosed to MDCH as required by 2 CFR Part 225, the MMSSSC and the MMHSSC.

Recommendation: Implement policies and procedures to report the ISF as required by the MMSSSC and the MMHSSC, and develop a historical computation or actuarial study to determine the appropriate funding balance for the ISF as required by the MMSSSC, MMHSSC, and 2 CFR Part 225.

Comments: MCCMH Finance recognizes that the ISF must be reported on the FSR regardless of its initial funding source, and that it must be historically or actuarially based.

Corrective Action: This correction has been addressed and changes already made. MCCMH established a formal ISF in FY 06 which has been consistently reported to MDCH on the FSR report. The amounts in the ISF are based on actuarial studies performed thus far by Milliman, the same firm that MDCH uses to develop MDCH CMH Capitation Rates. MCCMH will work to develop policies and procedures to document the process.

Anticipated Completion Date: Corrected. MCCMH anticipates the next actuarial study to be conducted this summer. Policies and procedures should be completed by August 2010.

MDCH Response: None.

Corrective Action Plan

Finding Number: 10

Page Reference: 14

Finding: **Improper Accounting for Unused Funds**

MCCMHSB improperly recorded unused funds from prior periods as a liability on their general ledger where no liability existed, which is in violation of the requirements of GAAP, the MMSSSC and the MMHSSC.

Recommendation: Implement policies and procedures to ensure all transactions are recorded in accordance with the requirements of GAAP, the MMSSSC and the MMHSSC. Also, write off this account balance as a prior period adjustment.

Comments: MCCMH Finance recognizes that unspent ABW funds of the current fiscal year become local funds in the following fiscal year.

Corrective Action: MCCMH will develop policies and procedures to ensure that all transactions are recorded in accordance with GAAP. The balance in question has been adjusted.

Anticipated Completion Date: August 2010.

MDCH Response: None.

Corrective Action Plan

Finding Number: 11

Page Reference: 15

Finding: **Differences Between the FSR and the Trial Balance**

MCCMHSB did not report revenues and expenditures correctly on the FSR as compared to the amounts stated on the trial balance, which is in violation of the MMSSSC and MMHSSC.

Recommendation: Implement policies and procedures to ensure that the revenues and expenditures reported on the FSR agree with the trial balance, as required by the MMSSSC and the MMHSSC.

Comments: MCCMH Finance staff review the trial balance to the FSR to ensure that revenues and/or expenditures are not missed. If MCCMH discovers that an adjustment is needed after the initial submission, MCCMH will issue a revised FSR to ensure that the final FSR and trial balance reconcile.

Corrective Action: MCCMH will establish written policies and procedures to address this issue so that there is not an unreconciled difference between the FSR and the trial balance. The new FSR reporting format is more comprehensive, and might be a useful tool to ensure that items are not missed.

Anticipated Completion Date: August 2010.

MDCH Response: None.

Corrective Action Plan

Finding Number: 12

Page Reference: 16

Finding: **Unallowable Rental Expenses**

MCCMHSB paid a subcontractor for unallowable rental expense and included the expense on the FYE 2006 FSR, which is in violation of the MMSSSC, MMHSSC, and federal cost principles.

Recommendation: Adopt policies and procedures to ensure that the FSR does not include expenses for unallowable rental costs, as required by federal cost principles and contractual agreements. Amend the FYE 2006 FSR and any other subsequent FSRs to remove unallowable rental costs and re-settle those years with MDCH.

Comments: The issue of the unallowable rental expense due to the Macomb Oakland Regional Center's property sale and lease-back arrangement had no financial implications in FY05. The issue came to light during the last quarter of FY06. At that point in time, MCCMH instructed Macomb Oakland Regional Center to remove any and all unallowable rental expenses from their final billing to MCCMH. Macomb Oakland Regional Center did so at that time. MCCMH did not report any unallowable expenses to MDCH on MCCMH's FY06 FSR.

Corrective Action: As indicated in Finding Number 2 and Finding Number 7, MCCMH will monitor Macomb Oakland Regional Center in a number of ways to ensure that MCCMH is aware of possible unallowable expenditures. In addition, MCCMH will continue to meet with Macomb Oakland Regional Center and discuss adherence to OMB Circular A-122 and OMB Circular A-87 as it relates to the contract between MCCMH and Macomb Oakland Regional Center. MCCMH will develop policies and procedures to ensure that the FSR does not include unallowable expenditures, including unallowable rental charges.

Anticipated Completion Date: August 2010.

MDCH Response: None.