STATE OF NEW JERSEY
OFFICE OF THE STATE COMPTROLLER

DEPARTMENT OF HUMAN SERVICES
DIVISION OF DEVELOPMENTAL DISABILITIES

FOLLOW-UP REPORT ON
OVERSIGHT OF THIRD-PARTY CONTRACTS

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COMPTROLLER

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F-05

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BACKGROUND, SCOPE AND OBJECTIVE

The Division of Developmental Disabilities (DDD) was created in 1985 within the Department of Human Services (DHS) to serve New Jersey residents with developmental disabilities. DDD currently serves nearly 43,000 developmentally disabled individuals (hereafter referred to as individuals). Approximately 2,650 individuals reside at State-run developmental centers that provide personal and medical care, training, therapy and supervision. More than 40,000 individuals live in a community setting, of whom nearly 30,000 reside at home with their families. The remaining individuals reside in various DDD-funded community settings.

DDD contracts with both for-profit and not-for-profit third-party providers that offer residential and non-residential services for those who are developmentally disabled. DDD administered approximately $926 million in contracts to 227 such third-party providers during Fiscal Year (FY) 2011.

Our initial audit, *Department of Human Services, Division of Developmental Disabilities*: *A Performance Audit of Oversight of Third-Party Contracts* (Report PA-05), issued on August 11, 2009, found that DDD did not adequately oversee the third-party contracts it awarded. Specifically, the audit found that DDD's system of monitoring was not designed to uncover inappropriate or unreasonable expenditures, or to ensure that services were being delivered as prescribed. As a result, taxpayer dollars were not being spent efficiently.

We made nine recommendations to enhance DDD's oversight of third-party contracts.

The objective of our follow-up engagement was to determine if DDD officials have implemented the nine recommendations contained in our initial audit report.

To make this determination, we reviewed, among other documents, applicable statutes, administrative code provisions, and DHS and DDD policies and procedures. We also reviewed the Corrective Action Plans provided to us by DDD officials in response to our audit recommendations. We also reviewed fiscal and programmatic aspects of DDD's oversight of four service providers (ARC of Camden County, Cerebral Palsy of North Jersey, Occupational Training Center of Burlington County and Willowglen Academy) that offer both residential and day programs. Such day programs (including adult training programs along with supported employment services) provide opportunities for individuals to explore personal interests, develop skills and make a contribution to their communities. These four providers had not been reviewed as part of our initial audit.

This follow-up engagement was performed in accordance with the State Comptroller's authority as set forth in N.J.S.A. 52:15C-1 et seq.

SUMMARY OF CONCLUSIONS

We found that DDD officials have made significant progress in implementing the recommendations contained in our initial audit report. As reflected in the chart below, of the nine audit recommendations, seven have been implemented and two have been partially implemented.

Area	Recommendation Number	Implemented	Partially Implemented	Not Implemented
Contract Monitoring	1		√	
	2	√		
	3	√		
	4	√		
Contracting Process	5		√	
	6	√		
	7	√		
	8	√		
	9	√		

Specifically, DDD has strengthened its monitoring of the fiscal and programmatic aspects of its provider contracts. Further, DDD has implemented measures that will allow it to identify problematic providers and more easily identify expenditures that are inappropriate or unreasonable. Such changes have helped DDD achieve greater fiscal accountability. We further note that DDD has made significant changes to its management structure since the issuance of our initial audit report. These changes in personnel have facilitated DDD's implementation of the recommended reforms.

We found, however, that DDD's case notes regarding client care still do not contain complete narrative information. To ensure compliance with our recommendations, DDD should continue to evaluate and refine its monitoring procedures concerning contract reimbursements and hold its case managers accountable for adequately completing case notes. In addition, while DDD is moving towards a fee-for-service payment model designed to streamline the contracting process, the fact that many clients with stable needs may remain within established contracts indefinitely is cause for concern.

STATUS OF INITIAL AUDIT RECOMMENDATIONS

Recommendation 1

Establish procedures to ensure that provider operations are effectively monitored for compliance with the CRM [Contract Reimbursement Manual] and CPIM [Contract Policy Information Manual].

Status: Partially Implemented

Our initial audit found that DDD did not adequately monitor the fiscal and programmatic aspects of its service provider contracts. Specifically, we identified the following deficiencies:

- Although DDD required contract administrators to conduct desk reviews, DDD did not have procedures detailing what the desk review should include or how a desk review should be conducted, resulting in perfunctory reviews which did not analyze specific expenditures. For example, general and administrative expenses for one provider exceeded 20 percent of its budget.

- Providers were not submitting required reports such as asset records, quarterly expenditure reports and annual audits.

- DDD was not closing out contracts in a timely manner, thereby limiting its ability to recover overpayments.

- Case managers' case notes regarding client care were either missing required narrative information or the information was copied word for word from previous reports. This failure called into question whether the case managers were actually conducting the required visits.

Our follow-up engagement revealed that since the time of our initial audit, DDD has taken several steps to enhance its monitoring of provider contracts. For example, DDD plans to increase the number of employees assigned to its contract administration unit. These personnel changes include providing technical and clerical support to the contract administrators, thereby enabling them to focus on the analytical aspects of reviewing provider expenditures rather than on administrative tasks. Moreover, DDD recently implemented a training program designed to provide guidance and instruction to case managers concerning the preparation of case notes. In addition, DDD has begun to implement contract monitoring procedures that are designed to enable it to identify potentially inappropriate or unreasonable expenditures before granting approval for reimbursement.

Based on our review of the four service providers previously referenced, we determined that:

- DDD's contract administrators now conduct reviews of providers' quarterly expenditure reports.

- Of 200 transactions we tested, there were no significant exceptions concerning unreasonable or inappropriate expenditures.

- General and administrative expenditures charged to the contracts ranged from 9.14 percent to 10.03 percent and averaged less than 10 percent.

- Quarterly expenditure reports were almost always submitted by the providers within the required 90 days, thereby enabling DDD to review them in a timely manner.

- All providers submitted asset records containing relevant information.

- One provider did not submit its audit within the required 120-day period. This provider submitted the audit 87 days late.

- Of 206 case manager notes we tested, 114 did not contain complete narrative information, with a few copied word for word from previous reports.

In addition, as a result of performing contract closeouts, DDD successfully collected nearly $18 million from expired contracts dating back as far as FY 2005. DDD continues to seek payment of an additional $3 million relating to the same period. These latter repayments are either being disputed by the provider or DDD is simply awaiting payment from the provider.

To ensure that contract administrators are reviewing contract-related expenditures in a manner that effectively mitigates the potential for inappropriate or unreasonable expenditures, DDD should periodically evaluate and refine its monitoring procedures. DDD also should hold its case managers accountable for adequately completing case notes, including all required narrative information.

Recommendation 2

Investigate the propriety of and, to the extent possible, pursue recovery of the $158,742 in undocumented and inappropriate costs cited in this report.

Status: Implemented

Upon testing a sample of expenditures, our initial audit found approximately $160,000 in a series of inappropriate and unreasonable expenditures incurred by a provider named Allies Inc. (Allies) and reimbursed by DDD. Some of the expenditures we found to be inappropriate and unreasonable included cruises to the Mediterranean and Caribbean ($111,851), purchase of a GPS navigation system ($1,999) and expenditures related to attending conferences in Nashville, Tennessee ($3,336) and Lake Buena Vista, Florida ($3,372).

In response to our audit, DDD hired the accounting firm of WithumSmith+Brown, PC (WSB) at a cost of $104,000 to conduct an audit of all of Allies' expenditures during the period July 1, 2006 through June 30, 2008. WSB's audit identified $1.141 million in expenditures for which Allies should not have been reimbursed by DDD. The categories of the adjustments cited by WSB are illustrated in the table below.

Adjustment Category	Adjustment Amount
Expenditures Over Budget	$586,995
Insufficient Documentation	$254,807
Vacation Expenditures	$217,168
Undocumented Expenditures	$55,012
Expenditures Unrelated to the Contract	$18,397
Expenditures Charged to the Incorrect Contract Year	$8,927
Total	**$1,141,306**

DDD has determined that Allies is responsible for returning $353,000 of the total amount cited by WSB. The recovery amount was calculated as follows:

- DDD initially determined that it should recover expenditures totaling approximately $545,000, which consisted of the Insufficient Documentation, Vacation Expenditures, Undocumented Expenditures and Expenditures Unrelated to the Contract adjustment categories listed in the above table. DDD subsequently reduced that amount by the $101,000 in payments made by individuals and employees to offset a portion of the cruise costs.

- WSB's audit also characterized approximately $587,000 as expenditures spent in excess of Allies' budget (Expenditures over Budget). However, DDD did not attempt to recover this amount since DDD had not reimbursed Allies for these expenditures. In addition, DDD did not attempt to recover approximately $9,000 that had been charged to the incorrect contract year.

- Subsequent to DDD's initial decision regarding the recovery amount, Allies provided additional supporting documentation related to approximately $91,000 of the questioned expenditures, thereby decreasing the final amount due to $353,000.

DDD has withheld the $353,000 from Allies' first contract payment for FY 2012.

Recommendation 3

In conjunction with the providers and the disabled community served by DDD, identify activities that meet the goal of accommodating the rights of disabled individuals while ensuring fiscal responsibility.

Status: Implemented

As noted above, our initial audit identified taxpayer-funded expenditures totaling $111,851 made by Allies to fund two cruises. Specifically, Allies organized a Mediterranean cruise for 25 employees (including management) and 23 individuals, and a Caribbean cruise for 31 employees (including management) and 33 individuals during FYs 2007 and 2008, respectively. Contrary to the provider's policy, it used DDD funds to pay for the cost of the cruises for its employees. In addition, DDD funds paid, in whole or in part, for such costs relating to 24 individuals.

DDD's revised policy now dictates that DDD will not fund travel expenditures for any staff member accompanying an individual on vacation. DDD will, however, continue to fund staff salaries in those circumstances. According to DDD, the policy decision to fund a staff member's salary, but not travel-related expenditures, recognizes both appropriate restraints on use of State funds and the importance of recreational activities notwithstanding one's developmental disability. DDD notes in this regard that the staffing needs attendant to one's disability continue regardless of the individual's physical location.

Similarly, DDD's revised policy now states that while an individual is on vacation DDD will provide funding only for those expenses DDD regularly pays for that individual in his or her residential placement.

Recommendation 4

Review the providers' adult training programs to ensure that IHP [Individual Habilitation Plan] requirements and employee requirements are being satisfied.

Status: Implemented

DDD's Office of Quality and Planning began completing site reviews of its day program sites in 2008. The focus of these reviews is to measure compliance with day program standards issued by DDD in 2007. Our initial audit found, however, that providers were not able to provide all of the documentation DDD required concerning both individuals and employees.

During our initial audit, we reviewed 371 client files and identified 134 that did not include required documentation considering the level of assistance needed by the individuals as set forth in their IHPs. For our follow-up engagement, we reviewed 132 client files and identified only 2 that did not include the required documentation for the level of assistance needed.

During our initial audit, we also reviewed 142 employee personnel files and identified 11 that did not include documentation indicating that the employee had completed mandatory pre-service trainings. For our follow-up engagement, our review of 62 personnel files at four providers did not reveal any such missing documentation.

Recommendation 5

Implement a system to competitively procure the services of third-party providers for contracts other than residential services. Limit the number of times a contract can be renewed without competition. Evaluate the feasibility of competitively bidding contracts for residential services.

Status: Partially Implemented

According to DDD, it is moving towards a fee-for-service payment model. Using this system, DDD has established rates for various services. DDD assesses an individual's need for services, including residential services, and assigns the individual a sum to pay for these services. Individuals then select from among DDD's pre-qualified service providers to obtain such services. DDD pays for these services through established provider contracts, but plans to transition to a system under which payments are made to providers from Medicaid directly.

As implementation of this fee-for-service system progresses, problems that we identified in DDD's history of non-competitively procured contracts should be rectified. DDD's fee-for-service solution introduces competition through individuals' choice of providers and through proactive outreach to ensure growing pools of qualified providers. DDD posts Requests for Qualifications inviting new providers to apply for qualification, and assists prospective providers concerning qualification procedures. DDD solicits qualified providers through e-mails it calls "e-blasts" that identify openings available for individuals who need services. These methods should shift DDD away from long-standing contracts with the same providers.

DDD is working to contain costs as it implements the fee-for-service changes. Present rates are lower than similar rates set in New York and Pennsylvania. DDD further ensures the appropriateness of charged rates through comparison with federally set reimbursement rates.

DDD was not able to project a date for full implementation of the fee-for-service payment method. Nor could the agency determine the exact number of individuals now operating under the fee-for-service model. Use of the fee-for-service payment process is presently restricted to new DDD clients and to those individuals seeking a change in services. As such, individuals with stable needs may stay within established contracts for non-residential services indefinitely. Accordingly, we are concerned that DDD is not fully embracing the recognized notion that competition in public contracting ensures the public receives the most economical price and also guards against "favoritism, improvidence, extravagance and corruption." Hillside v. Sternin, 25 N.J. 317, 322 (1957).

Our office will continue to monitor DDD's progress in implementing the new payment model.

Recommendation 6

Maintain relevant award documentation for each contract.

Status: Implemented

During our initial audit, DDD was unable to provide original procurement documents concerning four contracts that had been renewed annually over many years. DDD's document retention policy requires retention of award documents for ongoing contracts.

To determine if DDD now maintains relevant award documentation, we reviewed three contracts that resulted from a Request for Qualifications (RFQ) advertised by DDD in FY 2009. We found DDD's retention of documentation related to the contracts to be sufficient. The contract files each contained appropriate documentation including the public announcement of the contract opportunity, the RFQ, provider applications, the review panel's scoring sheets, DDD approvals and the resulting contracts.

Recommendation 7

Implement a contract-award evaluation process that considers the fiscal and programmatic performance of current providers. To facilitate this process, DDD must collect and maintain data related to the performance standards it has begun to establish.

Status: Implemented

Our initial audit found that DDD did not adequately consider provider performance before renewing a contract. DDD had not yet developed procedures to collect, compile and maintain relevant data in a central repository, in part due to a lack of information technology resources.

Beginning in September 2009, DHS's Office of Program Integrity and Accountability began posting on its website each quarter a performance review "dashboard" that includes information on each provider, including their licensing status, number of substantiated incidents and other performance measures. In addition, DDD's senior management now meets regularly with providers and their auditors to review specific performance and fiscal issues. According to DDD, it considers that information in the context of its contract renewal process.

Recommendation 8

Obtain and review the documentation necessary to support proposed contract modifications.

Status: Implemented

Our initial audit found that DDD was approving contract modifications for vehicle requests without obtaining asset records from the providers. As a result, DDD was approving the requests without knowing the number of vehicles already owned by the provider.

As part of our follow-up engagement, we reviewed all modifications to the four provider contracts previously referenced, including modifications related to the purchase of vehicles. All of the providers we reviewed had submitted asset records that included current vehicle ownership details. Our review also determined that DDD now requires additional details from providers in instances involving modifications for new vehicles. The provider must now explain how the vehicle will be used to fulfill its contractual obligations, as well as provide assurance that no one employee will be permanently assigned the vehicle. The provider must also demonstrate that it has sufficient funds to cover the vehicle's operating costs for the anticipated useful life of the vehicle and supply three written quotes for the same year, make, model and option package.

Providers looking to replace a vehicle must show that the current vehicle either: has an odometer reading that exceeds 125,000 miles; is at least ten years old;

requires repair costs that would exceed 50 percent of the current trade-in value; was totaled in an accident; or is deemed no longer safe to drive. If the provider receives DDD approval to purchase a vehicle, the cost of the vehicle, including all dealer fees and charges, may not exceed $25,000. This limitation excludes passenger vans and specialized vehicles for disabled individuals.

DDD is documenting all necessary information to support proposed contract modifications. DDD's process requires the contract administrator to review the fiscal aspects of the request to determine if the proposed cost is reasonable.

During our initial audit we also identified a situation that involved a provider requesting contract modifications that resulted in the provider increasing its overall contract amount by more than $1 million. This same provider ended the year by returning over $775,000 to DDD as a result of underspending. During our follow-up engagement, we did not identify any similar situations involving the four providers we reviewed.

Recommendation 9

Evaluate the payment methods under DDD's current contracts and consider the merits of the MPS [Milestone Payment System] form of contracting.

Status: Implemented

Our initial audit found that DDD funded each of its programs through either a general service contract or fee-for-service contract. General service contracts establish a fixed cost for all services provided to a specific number of individuals during the term of the contract. Fee-for-service contracts are structured to provide payments to providers based on the frequency and duration of each specific service provided.

We had found that as a result of its use of general service contracts, DDD was paying for unused slots at the ten adult training programs we reviewed. Specifically, we found that the adult training programs were being compensated for 405 contracted slots, but were providing services to an average daily attendance of only 323 individuals (80 percent). During our follow-up engagement, our review of attendance for 133 contracted slots at 5 adult training programs revealed an average attendance of 117 individuals (88 percent). To ensure that DDD maximizes its use of slots for which it has paid, it must continue to focus on identifying and eliminating chronically unused slots.

As discussed above concerning Recommendation 5, DDD is moving towards a fee-for-service payment model. DDD's transition from general service contracts to fee-for-service should result in DDD compensating providers only for services actually rendered.

Our initial audit also discussed several benefits associated with using the MPS contracting model. The MPS model uses an incentivized payment structure based on outcomes. Once performance outcomes are agreed to by the stakeholders, payments are made to the provider only after the users of the services pass pre-defined checkpoints or milestones on their way to the desired outcome.

DDD indicated that it has explored the merits of MPS. According to DDD, MPS is used solely in connection with supported employment programs. Nevertheless, DDD found that some of its components are worthy of greater consideration.

REPORTING REQUIREMENTS

We provided a draft copy of this report to DHS officials for their review and comment. Their comments were considered in preparing our final report and are attached as Appendix A.

DHS officials concurred with our conclusions. DHS noted that our 2009 audit "has had a positive impact in improving accountability and strengthening DDD's operation and delivery of services." In a few areas, DHS's comments provided clarification and additional information. Based on that information, we revised the text concerning Recommendation 5.

The Office of the State Comptroller is required by statute to monitor the implementation of our recommendations. To meet this requirement, DHS shall report periodically to this Office advising what additional steps it has taken to address the unresolved issues in this report. This Office will continue to monitor those steps.

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Lt. Governor

JENNIFER VELEZ
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October 6, 2011

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Re: Follow-Up Report on Oversight of Third-Party Contracts

Dear Mr. Boxer:

Thank you for the opportunity to review the referenced report. In general, the Division of Developmental Disabilities (DDD) agrees with the findings as documented in the follow-up report, i.e., seven (7) of the recommendations have been implemented while two (2) are partially implemented. There are select areas of the report, however, that we want to clarify and provide additional information for the formal record.

The report's Summary of Conclusions addresses case notes and the lack of complete narrative information. DDD's approach to case notes has been enhanced and made significantly stronger. A new Alternative Living Arrangement (ALA) Home Visit Report form was put in place on September 1, 2011. DDD's case managers across the State were trained on the new form during the months of July and August 2011. The form thoroughly documents outcomes from case managers' monitoring activities, as well as prompts case managers to focus on the providers' execution of regulatory requirements. In addition, ALA home visit dates and face-to-face visit dates, with accompanying notes, are being captured in a DDD information system for supervisory review, approval and tracking.

DDD appreciates the recognition of the progress made with regard to the contract "closeout" process since it was established in 2008. As part of this process, Contract Administrators have enhanced the monitoring of quarterly reports to ensure that expenditures are reviewed in a timely manner. These activities have resulted in a reduction of payments to agencies to offset anticipated underspending.

Recommendation #5 states, "Implement a system to competitively procure the services of third-party providers for contracts other than residential services. Limit the number of times a contract can be renewed without competition. Evaluate the feasibility of competitively bidding contracts for residential services." It is important to note that DDD's move toward a Fee for Service (FFS) system is not based on a desire to increase competition. Rather, a FFS methodology will streamline DDD's contracting and ensure equitable rates among provider agencies. With a FFS model, it will still be necessary to renew contracts. DDD believes the current system does foster competition as a consumer can choose from providers using a state-established fixed rate from a listing of qualified providers.

* Comment

Further, portions of Recommendation #5's narrative may lead the reader to believe that DDD is fully implementing FFS. While DDD's out-of-state contracts and a portion of in-state contracts are rate-based, movement toward a completely rate-based system is progressing in a methodical manner to avoid missteps.

Finally, with regard to Recommendation #9 - "Evaluate the payment methods under DDD's current contracts and consider the merits of the MPS [Milestone Payment System] form of contracting," DDD has developed a procedure targeting the elimination of unnecessary slots and continued monitoring of slot vacancies. DDD has surveyed other states and has found no other state is using MPS for similar contracts.

The Department of Human Services appreciates the enhancements to DDD's operations prompted by the Office of the State Comptroller's 2009 audit. We believe the audit has had a positive impact in improving accountability and strengthening DDD’s operation and delivery of services.

Sincerely,

Dawn Apgar

Dawn Apgar
Deputy Commissioner

c: Commissioner Velez
Assistant Commissioner Bailey
Shawn McInerney, Assistant Division Director, DDD
Manny Fernandez, Chief Financial Officer, DDD

*OSC Comment: We have revised our report based on information provided in the response.