DEPARTMENT OF HEALTH AND HUMAN SERVICES
OFFICE OF AUDIT SERVICES
233 NORTH MICHIGAN AVENUE
CHICAGO, ILLINOIS 60601

REGION V
OFFICE OF
INSPECTOR GENERAL

October 7, 2003

Report Number: A-05-03-00079

Dr. Jacqueline Scott, D.V.M, Ph.D.
Director, Office of Public Health Preparedness
Michigan Department of Community Health
33423 N. Martin Luther King Jr. Blvd.
P.O. Box 30195
Lansing, Michigan 48909

Dear Dr. Scott,

The attached report provides the results of our self-initiated review of the "State of Michigan's Efforts to Account for and Monitor Sub-recipients' Use of Bioterrorism Hospital Preparedness Program Funds."

Our objectives were to determine whether the Michigan Department of Community Health (State agency): (i) properly recorded, summarized and reported bioterrorism preparedness transactions in accordance with the terms and conditions of the cooperative agreements and (ii) had controls and procedures to monitor sub-recipient expenditures of Health Resources and Services Administration (HRSA) funds. In addition, we inquired as to whether Bioterrorism Hospital Preparedness Program (Program) funding supplanted funds previously provided by other organizational sources.

Based on our validation of the questionnaire completed by the State agency and our site visit, we determined that the State agency generally accounted for program funds in accordance with the terms and conditions of the cooperative agreement and applicable departmental regulations and guidelines. However, the State agency did not segregate expenditures by phase, within phase, or by priority area. Although segregation was not required, budget restrictions were specified in the cooperative agreement. State officials acknowledged the importance of tracking expenditures in order to comply with the budget restrictions. In addition, State officials indicated that that they were establishing procedures to comply with the requirements in the new HRSA Cooperative Agreement Guidance, effective August 31, 2003. The new guidelines require grantees to develop and maintain a financial accounting system capable of tracking expenditures by priority area, by critical benchmark, and by funds allocated to hospitals and other health care entities.

We also found the State agency had controls and procedures to monitor sub-recipient expenditures of Program funds. In response to our inquiry as to whether the State agency reduced funding to existing public health programs, State officials replied that Program funding had not been used to supplant existing State or local programs.

Final determination as to actions taken on all matters reported will be made by the HHS action official named below. We would appreciate your views and the status of any further action taken or contemplated on our recommendations within 15 days. Your response should present any comments or additional information that you believe may have a bearing on the final determination.

In accordance with the principles of the Freedom of Information Act, (5 U.S.C. 552, as amended by Public Law 104-231), Office of Inspector General reports are made available to members of the press and general public to the extent information contained therein is not subject to exemptions in the Act which the Department chooses to exercise. (See 45 CFR Part 5.)

If you have any questions or comments about this report, please contact Leon Siverhus, Audit Manager, at 651-290-3762.

To facilitate identification, please refer to Report Number A-05-03-00079 in all correspondence relating to this report.

Sincerely,

Paul Swanson

Paul Swanson
Regional Inspector General
for Audit Services

Enclosures – as stated

Direct Reply to HHS Action Official:
Nancy J. McGinness
Director, Office of Financial Policy and Oversight
Room 11A55, Parklawn Building
5600 Fishers Lane
Rockville, Maryland 20857

Department of Health and Human Services

OFFICE OF
INSPECTOR GENERAL

STATE OF MICHIGAN'S EFFORTS TO ACCOUNT FOR AND MONITOR SUB-RECIPIENTS' USE OF BIOTERRORISM HOSPITAL PREPAREDNESS PROGRAM FUNDS

OCTOBER 2003
A-05-03-00079

Office of Inspector General

The mission of the Office of Inspector General (OIG), as mandated by Public Law 95-452, as amended, is to protect the integrity of the Department of Health and Human Services (HHS) programs, as well as the health and welfare of beneficiaries served by those programs. This statutory mission is carried out through a nationwide network of audits, investigations, and inspections conducted by the following operating components:

Office of Audit Services

The OIG's Office of Audit Services (OAS) provides all auditing services for HHS, either by conducting audits with its own audit resources or by overseeing audit work done by others. Audits examine the performance of HHS programs and/or its grantees and contractors in carrying out their respective responsibilities and are intended to provide independent assessments of HHS programs and operations in order to reduce waste, abuse, and mismanagement and to promote economy and efficiency throughout the Department.

Office of Evaluation and Inspections

The OIG's Office of Evaluation and Inspections (OEI) conducts short-term management and program evaluations (called inspections) that focus on issues of concern to the Department, the Congress, and the public. The findings and recommendations contained in the inspections reports generate rapid, accurate, and up-to-date information on the efficiency, vulnerability, and effectiveness of departmental programs.

Office of Investigations

The OIG's Office of Investigations (OI) conducts criminal, civil, and administrative investigations of allegations of wrongdoing in HHS programs or to HHS beneficiaries and of unjust enrichment by providers. The investigative efforts of OI lead to criminal convictions, administrative sanctions, or civil monetary penalties. The OI also oversees State Medicaid fraud control units, which investigate and prosecute fraud and patient abuse in the Medicaid program.

Office of Counsel to the Inspector General

The Office of Counsel to the Inspector General (OCIG) provides general legal services to OIG, rendering advice and opinions on HHS programs and operations and providing all legal support in OIG's internal operations. The OCIG imposes program exclusions and civil monetary penalties on health care providers and litigates those actions within the Department. The OCIG also represents OIG in the global settlement of cases arising under the Civil False Claims Act, develops and monitors corporate integrity agreements, develops model compliance plans, renders advisory opinions on OIG sanctions to the health care community, and issues fraud alerts and other industry guidance.

Notices

THIS REPORT IS AVAILABLE TO THE PUBLIC
at http://oig.hhs.gov

In accordance with the principles of the Freedom of Information Act (5 U.S.C. 552, as amended by Public Law 104-231), Office of Inspector General, Office of Audit Services reports are made available to members of the public to the extent the information is not subject to exemptions in the act. (See 45 CFR Part 5.)

OAS FINDINGS AND OPINIONS

The designation of financial or management practices as questionable or a recommendation for the disallowance of costs incurred or claimed, as well as other conclusions and recommendations in this report, represent the findings and opinions of the HHS/OIG/OAS. Authorized officials of the HHS divisions will make final determination on these matters.

EXECUTIVE SUMMARY

OBJECTIVE

Our objectives were to determine whether the Michigan Department of Community Health (State agency): (i) properly recorded, summarized and reported bioterrorism preparedness transactions in accordance with the terms and conditions of the cooperative agreements and (ii) had controls and procedures to monitor sub-recipient expenditures of Health Resources and Services Administration (HRSA) funds. In addition, we inquired as to whether Bioterrorism Hospital Preparedness Program (Program) funding supplanted funds previously provided by other organizational sources.

FINDINGS

Based on our validation of the questionnaire completed by the State agency and our site visit, we determined that the State agency generally accounted for program funds in accordance with the terms and conditions of the cooperative agreement and applicable departmental regulations and guidelines. However, the State agency did not segregate expenditures by phase, within phase, or by priority area. Although segregation was not required, budget restrictions were specified in the cooperative agreement. State officials acknowledged the importance of tracking expenditures in order to comply with the budget restrictions. In addition, State officials indicated that that they were establishing procedures to comply with the requirements in the new HRSA Cooperative Agreement Guidance, effective August 31, 2003. The new guidelines require grantees to develop and maintain a financial accounting system capable of tracking expenditures by priority area, by critical benchmark, and by funds allocated to hospitals and other health care entities.

We also found the State agency had controls and procedures to monitor sub-recipient expenditures of Program funds. In response to our inquiry as to whether the State agency reduced funding to existing public health programs, State officials replied that Program funding had not been used to supplant existing State or local programs.

RECOMMENDATIONS

We recommend the State agency implement procedures to comply with the new requirements effective August 31, 2003 and begin tracking expenditures by priority area, critical benchmark, and by funds allocated to hospitals and other health care entities.

STATE AGENCY COMMENTS

In a written response to our draft report received September 3, 2003, the State agency concurred with our findings and recommendation. The State agency's response is included in its entirety as an appendix to this report.

TABLE OF CONTENTS

INTRODUCTION

BACKGROUND

The Program

Since September 2001, the U.S. Department of Health and Human Services has significantly increased its spending for public health preparedness and response to bioterrorism. For FYs 2002 and 2003, the Department awarded amounts for bioterrorism preparedness totaling $2.98 and $4.32 billion, respectively. Through this funding, some of the attention has been focused on the ability of hospitals and emergency medical services systems to respond to bioterrorist events.

Congress authorized funding to support activities related to countering potential biological threats to civilian populations under the Department of Defense and Emergency Supplemental Appropriations for Recovery from and Response to Terrorist Attacks on the United States Act, 2002, Public Law 107-117. As part of this initiative, the HRSA made available approximately $125 million in FY 2002 for cooperative agreements with State, territorial, and selected municipal offices of public health. The purpose of the Program is to upgrade the preparedness of the Nation's hospitals and collaborating entities to respond to bioterrorism.

The HRSA made awards to states and major local public health departments under Cooperative Agreement Guidance issued February 15, 2002. These awards provided funds for the development and implementation of regional plans to improve the capacity of hospitals, their emergency departments, outpatient centers, emergency medical systems and other collaborating health care entities for responding to incidents requiring mass immunization, treatment, isolation and quarantine in the aftermath of bioterrorism or other outbreaks of infectious disease.

Annual Program Funding

The Program year covered the period April 1, 2002 through March 31, 2003 and the funding totaled $125 million. It has since been extended to cover the period through March 31, 2004.

Budget Restrictions

During the program year, the cooperative agreements covered two phases. Phase I, *Needs Assessment, Planning and Initial Implementation*, provided 20 percent of the total award ($25 million) for immediate use. Up to one-half of Phase I funds could be used for development of implementation plans, with the remainder to be used for implementation of immediate needs. The remaining 80 percent of the total award ($100 million) was not made available until required implementation plans were approved by HRSA, at which point, Phase II, *Implementation*, could begin. Grantees were allowed to roll over unobligated Phase I funds to Phase II. They were required to allocate at least 80 percent of Phase II funds to hospitals and their collaborating entities through contractual awards to upgrade their abilities to respond to bioterrorist events. Funds expended for health department infrastructure and planning were not to exceed the remaining 20 percent of Phase II funds.

Eligible Recipients

Grant recipients included all 50 states, the District of Columbia, the commonwealths of Puerto Rico and the Northern Marianas Islands, American Samoa, Guam, the U.S. Virgin Islands, and the nation's three largest municipalities (New York, Chicago, and Los Angeles County). Those eligible to apply included the health departments of states or their bona fide agents. Individual hospitals, EMS systems, health centers and poison control centers work with the applicable health department for funding through the Program.

State Agency Funding

The Michigan Department of Community Health received approximately $4.1 million for the first year of the Program. According to State officials, the State agency had expended and obligated $2.12 and $1.98 million, respectively, as of June 30, 2003. Also as of June 30, 2003, State officials stated that all funds were obligated.

OBJECTIVE, SCOPE AND METHODOLOGY

Objectives

Our objectives were to determine whether the State agency: (i) properly recorded, summarized and reported bioterrorism preparedness transactions in accordance with the terms and conditions of the cooperative agreements and (ii) had controls and procedures to monitor sub-recipient expenditures of HRSA funds. In addition, we inquired as to whether Bioterrorism Hospital Preparedness Program funding supplanted funds previously provided by other organizational sources.

Scope

Our review was limited in scope, conducted for the purpose described above, and would not necessarily disclose all material weaknesses. Accordingly, we do not express an opinion on the system of internal accounting controls. In addition, we did not determine whether costs charged to the program were allowable.

Our audit included a review of State agency policies and procedures, financial reports, and accounting transactions during the period April 1, 2002 through March 31, 2003.

Methodology

We developed a questionnaire to address the objectives of the review. The questionnaire covered the areas of: (i) grantee organization, (ii) funding, (iii) accounting for expenditures, (iv) supplanting, and (v) sub-recipient monitoring. Prior to our fieldwork, we provided the questionnaire for the State agency to complete. During our on-site visit, we interviewed State officials and obtained supporting documentation to validate their responses to the questionnaire.

Fieldwork was conducted at the State agency offices in Lansing, Michigan and in our St. Paul, Minnesota field office during May and June 2003.

Our review was performed in accordance with generally accepted government auditing standards.

FINDINGS AND RECOMMENDATIONS

Based on our validation of the questionnaire completed by the State agency and our site visit, we determined that the State agency generally accounted for program funds in accordance with the terms and conditions of the cooperative agreement and applicable departmental regulations and guidelines. However, the State agency did not segregate expenditures by phase, within phase, or by priority area. Although segregation was not required, budget restrictions were specified in the cooperative agreement. State officials acknowledged the importance of tracking expenditures in order to comply with the budget restrictions. In addition, State officials indicated that they were establishing procedures to comply with the requirements in the new HRSA Cooperative Agreement Guidance, effective August 31, 2003. The new guidelines require grantees to develop and maintain a financial accounting system capable of tracking expenditures by priority area, by critical benchmark, and by funds allocated to hospitals and other health care entities.

We also found the State agency had controls and procedures to monitor sub-recipient expenditures of Program funds. In response to our inquiry as to whether the State agency reduced funding to existing public health programs, State officials replied that Program funding had not been used to supplant existing State or local programs.

Accounting for Expenditures

An essential aspect of the Program is the need for the grantee to accurately and fully account for bioterrorism funds. Accurate and complete accounting of Program funds provides the HRSA with a means to measure the extent that the program is being implemented and whether the objectives are being met. Although the State agency was not required to segregate expenditures in the accounting system by phase, within phase, or by priority area, there are budgeting restrictions set forth in the Cooperative Agreement Guidance and Summary Application Guidance for Award and First Allocation. Twenty percent of a grantee's total award will be made available in Phase I. Page 7 of the Cooperative Agreement Guidance states that indirect costs will be "limited to 10 percent of the Phase I and Phase II total."

Regarding Phase I funds:

> …Up to half of the Phase I funding may be allocated to planning and health department infrastructure to administer the cooperative agreement. At least half (50%) of the Phase I award must be allocated to hospitals and other health care entities to begin implementation of their plans….

Regarding Phase II funds, page 2 of the Summary Application Guidance for Award and First Allocation states:

> …Grantees will be required to allocate at least 80% of the Phase II funds to hospitals through written contractual agreements. To the extent justified, a portion of these funds could be made available to collaborating entities that improve hospital preparedness….

Without segregation of funds, the State agency has no assurance that funds expended do not exceed the budgeting restrictions set forth in the cooperative agreement. State officials acknowledged the importance of tracking expenditures in order to comply with the budget restrictions. Our review showed that the State agency was in compliance with the Phase I and II budget restrictions. We also noted indirect costs were claimed at 1.68 percent; significantly less than the 10 percent ceiling stipulated by the cooperative agreement.

In addition, State officials were addressing the new requirements in the 2003 HRSA Cooperative Agreement guidance, effective August 31, 2003. The guidance states the grantee must:

> …Develop and maintain a financial accounting system capable of tracking expenditures by priority area, by critical benchmark, and by funds allocated to hospitals and other health care entities….

According to State officials, Michigan will make every effort to comply with the new HRSA requirements for financial accountability. The State agency's budget office had already established dedicated Program Cost Accounts to track expenditures by priority area. They also stated that staff was aggressively working to develop and implement a system to mirror the State's system of financial accountability, and to develop it before the start of the State's fiscal year.

Sub-recipient Monitoring

Recipients of Program grant funds are required to monitor their sub-recipients. The PHS Grants Policy Statement requires that "grantees employ sound management practices to ensure that program objectives are met and that project funds are properly spent." It reiterates recipients must:

> …establish sound and effective business management systems to assure proper stewardship of funds and activities….

In addition, the Policy Statement further provides that grant requirements apply to subgrantees and contractors under the grants, as follows:

> …Where subgrants are authorized by the awarding office through regulations, program announcements, or through the approval of the grant application, the information contained in this publication also applies to subgrantees. The information would also apply to cost-type contractors under grants….

Based on the results of the questionnaire and interviews with State officials, we found that the State agency had adequate controls and procedures to monitor sub-recipient expenditures of

Program funds. State officials provided a detailed and thorough explanation with supporting documentation of their sub-recipient monitoring activities. As part of the monitoring process, the State agency requires sub-recipients to submit monthly Financial Status Reports. They also hold monthly meetings with the sub-recipients, perform on-site visits, and review sub-recipient purchase orders, invoices and other expenditure documentation.

Supplanting

Program funds were to be used to supplement current funding and focus on bioterrorism hospital preparedness activities under the HRSA Cooperative Agreement. Specifically, funds were not to be used to supplant existing Federal, State, or local public health funds available for emergency activities to combat threats to public health. Page 4 of the Cooperative Agreement Guidance states:

> …Given the responsibilities of Federal, State, and local governments to protect the public in the event of bioterrorism, funds from this grant must be used to supplement and not supplant the non-Federal funds that would otherwise be made available for this activity….

OMB Circular A-87 also states:

> …funds are not to be used for general expenses required to carry out other responsibilities of a State or its sub-recipients….

In response to our inquiry as to whether the State agency reduced funding to existing public health programs, State officials replied that Program funding had not been used to supplant existing State or local programs.

RECOMMENDATION

We recommend the State agency implement procedures to comply with the new requirements, effective August 31, 2003, and begin tracking expenditures by priority area, critical benchmark, and by funds allocated to hospitals and other health care entities.

STATE AGENCY COMMENTS

In a written response to our draft report received September 3, 2003, the State agency concurred with our findings and recommendation. The State agency's response is included in its entirety as an appendix to this report.

APPENDIX

JENNIFER M. GRANHOLM
GOVERNOR

STATE OF MICHIGAN
DEPARTMENT OF COMMUNITY HEALTH
LANSING

JANET OLSZEWSKI
DIRECTOR

Report Number A-05-03-00079

Mr. Paul Swanson, Regional Inspector General for Audit Services
Department of Health and Human Services
Office of Audit Services
233 North Michigan Avenue
Chicago, Illinois 60601

Dear Mr. Swanson

In response to receipt and review of the draft report of recent audit of the Michigan Department of Community Health, Office of Public Health Preparedness use and disposition of federal funds received under the Bioterrorism Hospital Preparedness Program Grant, we concur with the factual content of the report and accept the reasonableness of the recommendation presented.

We welcome the findings that we are in compliance with the requirements of grant participation and reconfirm policies are being implemented for the new grant cycle (August 31, 2003), which will fully comply with new requirements to track all grant related expenditures by priority area, critical benchmark, and by funds allocated to hospitals and other health care entities. Adherence to these accounting policies will be required of both the state accounting system and that of all sub-recipients of grant funding.

Thank you.

Sincerely,

Jacqueline S. Scott, D.V.M., Ph.D.
Director
Office of Public Health Preparedness
Telephone: 517-335-8150
Fax: 517-335-9434
Email: scottjac@michigan.gov

ACKNOWLEDGEMENTS

This report was prepared under the direction of Paul Swanson, Regional Inspector General for Audit Services. Other principal Office of Audit Services staff who contributed include:

Leon Siverhus, *Audit Manager*
Brent Storhaug, *Senior Auditor*
Shirley Loos, *Auditor*

For information or copies of this report, please contact the Office of Inspector General's Public Affairs office at (202) 619-1343.