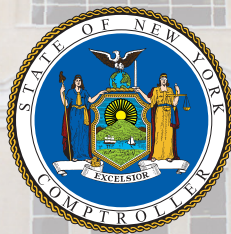




New York State Office of Mental Health

Contracts for Personal and Miscellaneous Services

Report 2009-S-42



Thomas P. DiNapoli

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State of New York Office of the State Comptroller

Division of State Government Accountability

August 26, 2010

Michael Hogan
Commissioner
New York State Office of Mental Health
44 Holland Avenue
Albany, NY 12229

Dear Mr. Hogan:

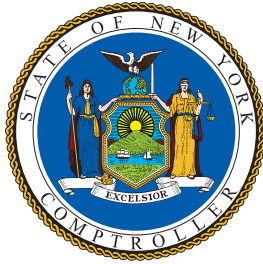
The Office of the State Comptroller is committed to helping State agencies, public authorities and local government agencies manage government resources efficiently and effectively and, by so doing, providing accountability for tax dollars spent to support government operations. The Comptroller oversees the fiscal affairs of State agencies, public authorities and local government agencies, as well as their compliance with relevant statutes and their observance of good business practices. This fiscal oversight is accomplished, in part, through our audits, which identify opportunities for improving operations. Audits can also identify strategies for reducing costs and strengthening controls that are intended to safeguard assets.

Following is a report of our audit of *Contracts for Personal and Miscellaneous Services*. The audit was performed pursuant to the State Comptroller's authority as set forth in Article V, Section 1 of the State Constitution and Article II, Section 8 of the State Finance Law.

This audit's results and recommendations are resources for you to use in effectively managing your operations and in meeting the expectations of taxpayers. If you have any questions about this report, please feel free to contact us.

Respectfully submitted,

*Office of the State Comptroller
Division of State Government Accountability*



State of New York

Office of the State Comptroller

EXECUTIVE SUMMARY

Audit Objectives

One objective of our audit was to determine whether the Office of Mental Health (OMH) justified the need to contract for personal and miscellaneous services. Another objective was to determine whether OMH periodically reassessed personal and miscellaneous services contracts to identify what work could be deferred, eliminated, or reduced to save State funds.

Audit Results - Summary

Various directives from the New York State Division of the Budget and the Governor's Office include the need for State agencies to justify their personal and miscellaneous service contracts (Service Contracts) and to reassess whether they can be deferred, eliminated or reduced to help achieve overall budgetary reductions and related cost savings. These directives have added significance because in August of 2008 the Governor required State agencies to achieve spending reductions of 10.35 percent for State fiscal year 2008-09. For the period April 1, 2006 through March 31, 2009, OMH had 819 State-funded Service Contracts valued at \$974 million.

We found that OMH generally did not justify the need for new or renewed Service Contracts. For example, we reviewed a sample of 50 OMH Service Contracts valued at \$61.7 million and found OMH did not have documented justification for the need for 35 of these contracts valued at \$48.2 million. We believe that supporting documentation is necessary to adequately establish that OMH had reached the correct conclusions about the need for contracted services and the extent of opportunity for reducing contract scope to achieve savings.

OMH did not provide documentation to support that it reassessed all of its Service Contracts. Therefore, OMH may be missing opportunities to further reduce costs and save State funds. If it attained a 10 percent reduction in the remaining value of the Service Contracts that were active as of November 30, 2009, OMH could realize savings of more than \$22 million.

Our report contains two recommendations for improving OMH efforts to attain savings through justification and reassessment of Service Contracts. In responding to our audit, OMH officials generally agreed with our recommendations and outlined actions they plan to take to implement them. However, they also expressed confidence in the appropriateness of OMH's existing pool of Service Contracts, noting that evaluating the need for contracts is a ongoing, multi-layered process involving fiscal and programmatic staff at both the Central Office and local level. They pointed out that OMH has always been able to meet its spending

reduction targets and stressed that a decision to reduce reliance on a Service Contract is often a budgetary decision to refrain from making additional procurements, than a formal cancellation or modification of an existing contract.

This report, dated August 26, 2010, is available on our website at: <http://www.osc.state.ny.us>.

Add or update your mailing list address by contacting us at: (518) 474-3271 or

Office of the State Comptroller

Division of State Government Accountability

110 State Street, 11th Floor

Albany, NY 12236

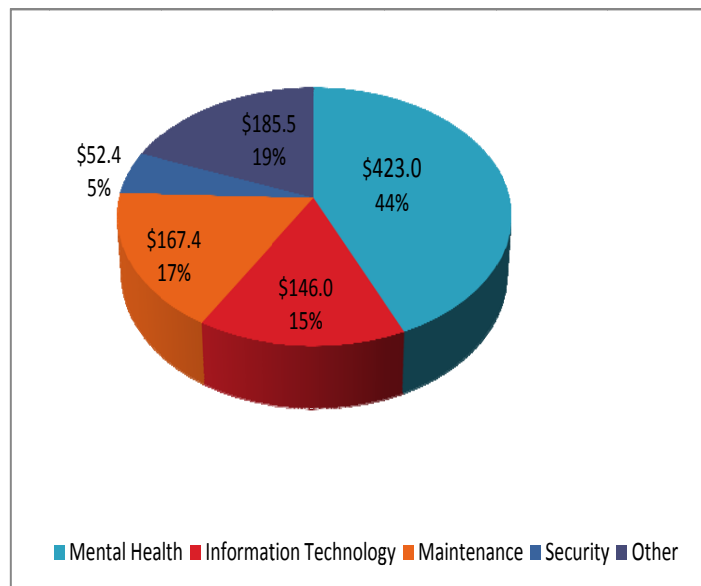
Introduction

Background

The mission of the Office of Mental Health (OMH) is to promote the mental health of all New Yorkers with a particular focus on providing hope and recovery for adults with serious mental illness and children with serious emotional disturbances. It operates psychiatric centers across the State, and also regulates, certifies and oversees more than 2,500 programs that are operated by local governments and not-for-profit agencies. These programs include various inpatient and outpatient programs, as well as emergency, community support, residential and family care programs that serve more than 687,000 individuals annually.

According to its records, OMH had 819 active Service Contracts with a total value of more than \$974 million during the period April 1, 2006 through March 31, 2009. These contracts are categorized in the following chart:

Contracts Awarded
(\$ in millions and % of total)



The following directives issued from the New York State Division of the Budget and the Governor set forth expectations for State agencies to make sure that expenditures, including Service Contracts, are justified and are periodically reassessed:

- State Budget Bulletin H-1025, which became effective July 31, 2003, requires agency management to review all contracts (both new and renewals), including those that involve service delivery to affected citizens, to ensure that lower priority, overlapping or otherwise inefficient activities are eliminated. This Bulletin was in effect until the end of our audit fieldwork in September 2009.
- State Budget Bulletin B-1178, which became effective April 21, 2008, requires agency management to scrutinize all programs and operations to identify opportunities to eliminate less important activities and spending on non-essential items. It further requires agencies to develop plans to identify cost-savings and recurring savings. In this regard, under B-1178, agencies are required to scrutinize spending for contractual services among several other items. Furthermore, B-1178 requires agencies to develop plans that include a framework for continuing fiscal year 2008-09 savings through to fiscal year 2011-12.
- State Budget Bulletin B-1183, which became effective August 21, 2008, requires State agencies to review all agency programs and operations to identify opportunities for eliminating less essential activities and spending on non essential items.
- On June 4, 2008, the Governor issued Executive Order No. 6 (Order) requiring State agencies not to enter into Qualified Personal Services Contracts (e.g. engineering, research and analysis, data processing) exceeding \$1 million or more of personal service over any 12-month period unless the agency first determined that: (a) the contractor can carry out the task more efficiently or effectively than state employees; (b) the contractor can carry out the task for a lower cost than state employees; or (c) the contract is necessary to protect the public health or safety, or is for some other compelling reason.

Both the Budget Bulletins and the Order have added significance given the State's increasing fiscal difficulties. In this regard, in August 2008, the Governor directed that State agencies evaluate all programs and operations to identify opportunities to eliminate less essential activities and achieve spending reductions of 10.35 percent in State fiscal year 2008-09. As part of this responsibility, State agencies were to develop a detailed plan that described the agency's proposed process for reviewing/approving non-personal service spending. Agencies were expected to balance personal service and non-personal service reductions so as to not disproportionately impact either, and to ensure recurring savings in both categories.

Audit Scope and Methodology

One objective of our audit was to determine whether OMH justified the need to contract out for personal and miscellaneous services (Service Contracts). Another objective was to determine whether OMH periodically reassessed Service Contracts to identify what work can be deferred, eliminated or reduced to help cope with the State's fiscal difficulties. For the purposes of our audit, Service Contracts are those in which the majority of the costs associated with the contracts are for services and labor. We did not include contracts for commodities or capital construction. Our audit period was April 1, 2006 through November 30, 2009.

To achieve our objectives, we interviewed OMH personnel, and reviewed contracts and other supporting documentation provided by OMH. We also reviewed relevant State laws, the Order and Budget Bulletins. We selected a judgmental sample of 50 Service Contracts totaling \$61.7 million from the 819 active contracts during our audit period. We selected our sample from contracts over \$50,000. The selection includes contracts for mental health services, information technology, maintenance, security, and other services.

We conducted our performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

In addition to being the State Auditor, the Comptroller performs certain other constitutionally and statutorily mandated duties as the chief fiscal officer of New York State. These include operating the State's accounting system; preparing the State's financial statements; and approving State contracts, refunds, and other payments. In addition, the Comptroller appoints members to certain boards, commissions and public authorities, some of whom have minority voting rights. These duties may be considered management functions for purposes of evaluating organizational independence under generally accepted government auditing standards. In our opinion, these functions do not affect our ability to conduct independent audits of program performance

Authority

This audit was performed pursuant to the State Comptroller's authority as set forth in Article V, Section 1 of the State Constitution and Article II, Section 8 of the State Finance Law.

**Reporting
Requirements**

A draft copy of this report was provided to OMH officials for their review and comment. Their comments were considered in preparing this final report and are attached in their entirety at the end of the report.

Within 90 days of the final release of this report, as required by Section 170 of the Executive Law, the Commissioner of the Office of Mental Health shall report to the Governor, the State Comptroller, and the leaders of the Legislature and fiscal committees, advising what steps were taken to implement the recommendations contained herein, and where recommendations were not implemented, the reasons why.

**Contributors to
the Report**

Major contributors to this report include Frank Patone, Michael Solomon, Santo Rendon, Salvatore D'Amato, Richard Canfield, Raymond Louie, Unal Sumerkan and Dana Newhouse.

Audit Findings and Recommendations

Justification of Service Contracts

We selected a sample of 50 Service Contracts and reviewed available documentation to determine whether the need for the services and the decision to contract for services was justified with supporting documentation. OMH was able to demonstrate that it had formally evaluated and justified the need for only 15 of these contracts totaling \$13.5 million. However, the Department did not have documentation showing that it formally evaluated the justification for the remaining 35 contracts, which totaled \$48.2 million. These contracts involved mental health services, information technology, maintenance, and security services.

OMH officials agreed that all of the decisions pertaining to contracting for Services were not documented, but indicated that this is not a feasible task, as decisions are made at many levels in many forms. They also believe they have effectively communicated the intent of the budget bulletins to all OMH divisions and facilities. However, we did not find sufficient evidence that OMH had contracted out only when there was a clearly documented need for the services.

We acknowledge that there are times when outside consultants must be hired. However, even in these cases, a documented analysis is important to fully support that OMH's conclusions are correct and that opportunities and options for cost savings have been fully considered.

Reassessment of Service Contracts

Based upon our review of OMH's efforts to scrutinize Service Contract spending, we believe additional savings opportunities may be possible. We found that OMH has not performed the periodic reviews required by the Division of the Budget (DOB), nor has it performed a comprehensive assessment of existing Service Contracts to prioritize their importance or determine whether any can be cut back, postponed or eliminated. We recommend that OMH comply with the Bulletins issued by DOB and perform the required top-to-bottom reviews of all Service Contracts. OMH officials noted that they have met the overall reduced spending targets set for OMH by the Governor.

As of November 30, 2009, OMH had expended about \$386 million against the \$607 million total value of existing Service Contracts; leaving over \$221 million left to be spent. If OMH officials could achieve just a 10 percent spending reduction on the remaining balances of these contracts,

as it did with its other budgeted costs in 2008 and 2009, it could realize more than \$22 million in cost savings

In responding to our audit, OMH officials expressed confidence in the appropriateness of their existing pool of Service Contracts, noting that assessing the need for contracts is a ongoing, multi-layered process involving fiscal and programmatic staff at both the Central Office and local level. They pointed out that OMH has always been able to meet its spending reduction targets and stressed that a decision to reduce reliance on a Service Contract is often a budgetary decision to refrain from making additional procurements, rather than a formal cancellation or modification of an existing contract.

- Recommendations**
1. Executive management should communicate to appropriate staff the requirement to support Service Contracts with written justifications of the need for the service, the appropriate level of service, and the need to contract out.
 2. Instruct managers to periodically reassess all Service Contracts to identify opportunities to suspend, eliminate, reduce or bring them in-house, and to document their determinations.

Agency Comments



State of New York
David A. Paterson
Governor



Office of Mental Health
44 Holland Avenue
Albany, New York 12229
www.omh.state.ny.us

July 2, 2010

Frank Patone, CPA
Audit Director
Office of the State Comptroller
Division of State Government Accountability
123 William Street, 21st Floor
New York, NY 10038

Dear Mr. Patone:

The Office of Mental Health has reviewed the draft audit report entitled, Office of Mental Health: Contracts for Personal and Miscellaneous Services (2009-S-42). Our comments to the findings and recommendations contained in the report are enclosed.

The Office of Mental Health appreciates the Office of the State Comptroller's efforts to recommend improvements in our operations.

Many thanks for your continued help and cooperation.

Sincerely yours,

Bruce E. Feig
Executive Deputy Commissioner

Enclosure

AN EQUAL OPPORTUNITY/AFFIRMATIVE ACTION EMPLOYER



OMH 26.01 (3/08)

**OFFICE OF MENTAL HEALTH
RESPONSE TO THE OFFICE OF THE STATE COMPTROLLER
DRAFT REPORT 2009-S-42
CONTRACTS FOR PERSONAL AND MISCELLANEOUS SERVICES**

OMH officials have reviewed the findings and recommendations in the Office of the State Comptroller's (OSC) draft report entitled, Office of Mental Health: Contracts for Personal and Miscellaneous Services. OMH recognizes that the audit results are intended as a resource to assist us in improving our operations and will take action to implement OSC's recommendations. However, we also have some concerns about assertions made in the report.

OMH STATE OPERATIONS SPENDING

This audit asserts that by not reassessing all of its contracts, OMH may be missing opportunities to further reduce costs and save state funds. Further it states that more than \$22 million in contract savings could be achieved if it reduced the remaining value of its contracts by 10 percent. We respectfully disagree. Due to their health and safety aspects, these contracts cannot simply be reduced by 10 percent. Moreover, as described below, OMH has taken, and will continue to pursue, opportunities to limit or reduce contract expenditures.

*
Comment

Since the beginning of the fiscal crisis about two years ago, OMH has taken its share of spending and workforce reductions. As the audit report indicates, OMH has met all cut targets set by the Division of Budget (DOB) and Governor's Office. This includes the FY 2008-09 10.35 percent savings reductions and FY 2009-10 Deficit Reduction Plan. Furthermore, OMH met its Personal Services savings targets as part of the FY 2009-10 Voluntary Severance Plan. OMH has a good track record of spending within appropriation amounts and meeting cash targets established by DOB.

Simply stated, OMH has fewer resources today than two years ago to meet the needs of the clients it serves. A comparison of actual annual salaried positions from March 31, 2008 to March 31, 2010 demonstrates that OMH has lost 904 (or 5.3 percent) full-time equivalent positions – from 17,026 to 16,122. Furthermore, actual non-personal services disbursements (from the Mental Hygiene Program Fund and Patient Income Account) have been reduced over that same period by \$11.5 million (or 3.9 percent) – from \$294.8 million to \$283.3 million – in spite of inflationary trends. A significant part of non-personal services spending supports items including but not limited to: patient medications, utilities, patient food, patient medical and clinical services such as outside hospital care, and asset maintenance. Due to the State's continuing fiscal crisis, OMH fully anticipates future deficit reduction activities. Although difficult choices will need to be made, OMH will continue to make them by prioritizing expenses of all types including personal services and non-personal services funding.

* See State Comptroller's Comment on page 21.

OMH is concerned with OSC's assertion that standing personal and miscellaneous services contracts can be simply cut by 10 percent to generate a savings of \$22 million. This statement is without regard to an assessment of the criticality of such services. These contracts are managed by OMH's decentralized network of 27 hospitals and research institutes, along with various central office program divisions. Although all are considered service contracts they have varied purposes including, but not limited to, the provision of medical services to patients involving psychiatry and nursing; maintenance of facility infrastructure (such as boilers, elevators and fire alarms); patient support services; and information technology services. To suggest that OMH reduce the remaining value of these contracts by 10 percent in light of significant reductions already effectuated does not recognize the efforts already undertaken within the agency.

CONTRACT ASSESSMENT PROCESS

As of June 1, 2010, OMH managed 475 personal and miscellaneous services contracts with an aggregate life value of \$741 million. These contracts are intended to support the health and safety needs of patients and to assist OMH in meeting its core mission of promoting the mental health of all New Yorkers with a particular focus on facilitating hope and recovery of adults with serious mental illnesses and children with serious emotional disturbances. Many of these contracts are also essential in ensuring that OMH meets minimum national accreditation standards set by the Joint Commission and the Centers for Medicare and Medicaid Services. This accreditation is necessary for maintaining about \$1.2 billion in annual patient revenue streams to the State.

When a contract is established at a certain value (which includes an annual budget), the amount is based on what OMH believes it needs at the time. However, for many contracts, the full value is not spent. In the audit, OSC asserts that *"As of November 30, 2009, OMH had expended about \$386 million against the \$607 million total value of existing Service Contracts; leaving \$221 million left to be spent."* OSC states that if just 10 percent were reduced from the unspent portion of these contracts, \$22 million could be saved. However, what OSC does not point out is that the full value of many contracts is not spent. OMH considers this underspending when developing annual budgets as well as responding to requests for budget reductions.

In fact, of the 50 contracts sampled by OSC, 23 contracts had expired as of December 31, 2009. Of those 23 contracts, eight expended at 80 percent or less of their full funding authorization. Six of the eight expended at less than 50 percent of full value. Those 23 expired contracts had a life value of \$19.255 million. However, actual expenditures against them totaled \$15.082 million, or only 78 percent of life value.

Performing a review to determine whether or not such contracts are needed or can be reduced is a multi-layered process. It includes the contract manager and Central Office program coordinators and leaders who assess the programmatic need of such a contract. Also involved are fiscal managers who assess whether funding exists to support such a contract. This is an

iterative process with no central repository for all the justification supporting the need of a contract.

An example of OMH's continuing assessment of the utilization of contracts includes our participation in information technology in-sourcing initiatives. OMH is actively assessing information technology contracts that can be converted to functions performed by less costly State employees as part of the initiative set forth in Chapter 500 of the Laws of 2009. Moreover, the FY 2010-11 Executive Recommendation includes a proposal to maximize 13 consultant contract items by converting them into 19 State positions at no additional cost to the State.

It is the intent of OMH to maximize the use of its available workforce, but sometimes service contracts are necessary to accomplish a goal or meet a critical need. Contractual services fall into two basic categories: 1) services that require a specialized expertise or unique skill set that cannot be handled by Agency staff; and 2) services that under optimal circumstances would most likely be handled by Agency staff, but for budget and local considerations. The vast majority of services are provided by Agency staff.

- 1) Expert Services - OMH contracts out for certain functions that facility staff simply aren't trained or licensed to handle. To carry out such duties requires an expertise that is not consistent with the core mission of the Agency, but vital to the safe day-to-day operation of the hospitals. Examples of such services include asset maintenance agreements to support the safe operation of hospital infrastructure (e.g., elevators, generators, fire alarms, and HVAC); pest control which requires a special certification in order to render services in hospital settings; refuse and hazardous waste removal; etc.
- 2) Agency Services - Under optimal circumstances, OMH would employ a full complement of staff necessary to support core operations. However, as a result of a myriad of budget decisions over the years and local conditions, there are necessary choices OMH hospitals and Central Office must make to ensure that the work gets done. Trade-offs between hiring staff into State positions versus seeking service contracts with external entities occur routinely. As a result, there are several filters to determine whether it makes the most sense to utilize a State employee or enter into a contractual agreement. Considerations include:
 - Can a State employee be recruited? Many State positions such as psychiatrists and nurses are hard-to-recruit due to competition with the private sector.
 - Is the position only needed on a part-time or on a sporadic basis? It is not efficient for certain positions to be filled by State employees since a full-time presence is not always needed.
 - Is it less costly to contract?
 - Is the contract necessary to cover for State staff leave (e.g., maternity, medical, etc.)?
 - Is there sufficient authorized fill capacity to hire a State employee?

- Where is the location of the service needed? Many OMH community programs are not co-located with their host facility. As a result, contracts for certain support services are more efficient than having a State staff person travel from the host facility.
- Is an employee needed for a project or on a permanent basis? Occasionally, a need for services is project-driven requiring only a temporary commitment.

OMH appreciates OSC's review of its operations and contracting processes. As a result of the current fiscal climate, OMH expects the Executive Branch to implement future deficit reduction plans and will continue to assess all spending to ensure the delivery of most critical services while meeting its financial targets. We must, however, reiterate that OSC's assertion, that \$22 million in savings is available by simply reducing service contracts 10 percent, is not realistic due to the health and safety aspects of many of our contract arrangements.

*

Comment

OMH'S RESPONSE TO OSC'S RECOMMENDATIONS

OSC Recommendation 1:

Executive management should communicate to appropriate staff the requirement to support Service Contracts with written justifications of the need for the service, the appropriate level of service, and the need to contract out.

OMH Response:

Beginning with the 2010-11 Spending Plan process, OMH's State Budget & Financial Management Services Group is using a standardized form that facilities and central office divisions must complete when requesting to enter into a new, renewed or re-bid contract valued at more than \$15,000. The form asks several questions related to the contract. Some questions include an overview of the contract's intent; for renewals, if the scope of work is changing; justification of cost; if there were other more cost-effective alternatives to the contract; and if estimated annual contractual personal services spending is more than \$1 million then Executive Order 6 applies. This form will bring key elements of consideration into one document.

OSC Recommendation 2:

Instruct managers to periodically reassess all Service Contracts to identify opportunities to suspend, eliminate, reduce or bring them in-house, and to document their determinations.

OMH Response:

As part of the annual spending plan process for facilities and program divisions, OMH State Budget Services will disseminate explicit instructions to staff that they should be reviewing service contracts for opportunities to suspend, eliminate, reduce or bring functions in-house, and to document their determinations.

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* See State Comptroller's Comment on page 21.

State Comptroller's Comment

We recognize the critical nature many contracts play in ensuring proper patient care and addressing other life-safety concerns. In that regard, we are not suggesting that OMH should universally reduce the value of each and every contract by 10 percent, but rather that if management were to examine all contracts for necessity, the aggregate savings identified could amount to 10 percent of current contract values. The fact that OMH cites a group of contracts from our sample which expired in 2009 with an average of only 78 percent expended, shows that a 10 percent reduction is achievable and may actually be conservative.