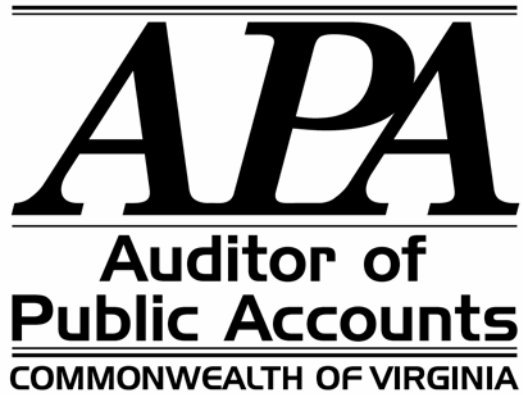
DEPARTMENT OF MENTAL HEALTH, MENTAL RETARDATION, AND SUBSTANCE ABUSE SERVICES

REPORT ON AUDIT FOR THE YEAR ENDED ENDED JUNE 30, 2006



AUDIT SUMMARY

Our audit of the Department of Mental Health, Mental Retardation, and Substance Abuse Services (Department) for the year ending June 30, 2006, found:

- proper recording and reporting of all transactions, in all material respects, in the Commonwealth Accounting and Reporting System and the Department's internal accounting system;

- matters involving internal control that require management's attention and corrective action;

- instances of noncompliance with applicable laws and regulations or other matters that are required to be reported; and

- adequate corrective action of prior year findings.

Included in our recommendations, the Department should:

- develop policies and procedures and adhere to them to assist in monitoring Community Service Boards; and
- allocate the time and resources to complete a comprehensive security awareness program.

These matters are discussed in detail in the section of our report entitled "Audit Findings and Recommendations, along with other recommendations the Department should consider.

In addition, we included a risk alert which discusses issues that require the action of either another agency, outside party or the method by which the Commonwealth of Virginia conducts its operations. The following matter represents a risk to the Department but the Department must rely on the Virginia Information Technologies Agency (VITA) to address the risk.

- Obtain Assurance for Infrastructure Security

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AUDIT FINDINGS AND RECOMMENDATIONS

Risk Alert

During the course of our audits, we encounter issues that are beyond the corrective action of management and require the action of either another agency, outside party, or the method by which the Commonwealth conducts its operations.

Obtain Security Risk Assurance for Infrastructure

The Commissioner has responsibility for the security and safeguarding of all of the Department's information technology assets, systems and information. Over the past three years, the Commonwealth has moved the information technology infrastructure supporting these databases to the Virginia Information Technologies Agency (VITA). In this environment, VITA and the Commissioner clearly share responsibility for the security of the Department's information technology assets, systems and information and must provide mutual assurance of this safeguarding.

The Department has provided VITA with all the documentation required to make this assessment. However, VITA has not been able to provide the Department with assurance that they can provide hardware and software configurations that satisfy these requirements and appropriate controls to secure information technology assets, systems, and information.

Therefore, the Department cannot fulfill their responsibilities stated in the state policy, which will put its information technology assets, systems, and information at risk. As such, VITA needs to provide assurance to the Department that appropriate security is available to meet the Department's information security requirements.

Internal Control and Compliance Findings and Recommendations

Strengthen Monitoring of the Community Services Boards

The Department pays over $200 million in state funds and $59 million in federal funds to Community Services Boards (Boards) each year to provide services to individuals within the community. The federal government requires that the Department monitor the Boards to ensure they meet programmatic and financial federal grant requirements.

Recently, the Department changed their process for monitoring the Boards by redistributing different monitoring responsibilities to various divisions. The Department is attempting to monitor the Boards without documented policies and procedures describing what the different divisions will do and how they will work together to resolve problems or issues with the Boards.

Documented policies and procedures prevent overlaps and/or gaps in coverage, help divisions coordinate their efforts, and determine responsibility for resolving issues and problems in a timely manner. We recommend the Department develop policies and procedures and adhere to them to assist in the monitoring process. The procedures should cover how the divisions will communicate their results, as issues affecting one or more of the divisions may indicate a larger problem. The Department can use these policies and procedures as evidence that it is fulfilling its monitoring responsibility as required by the federal grant. Monitoring and providing oversight to the Boards will become more critical in the future as the Boards are expecting to receive more state and federal funds as part of the current transformation to move more individuals out of state-run institutions and into community programs administered by the Boards.

Expand Security Awareness Training Program

The Department does not have a comprehensive Security Awareness Training Program that meets the requirements of the Commonwealth's Information Security Standard. Users within the Department need to be aware of the sensitivity of the Department's information resources and their responsibility in maintaining the security of these resources in order to minimize the risk of loss or unauthorized alteration or disclosure.

While the Department provides training related to the Health Insurance Portability and Accountability Act (HIPAA), the Department should expand their Security Awareness Training Program to include the following at minimum:

- both general and position appropriate security awareness content
- approval by the Agency Information Security Officer
- specified timeframes for receiving training
- documented on an auditable medium

The Department should allocate the time and resources to complete a comprehensive security awareness program that considers its unique environment, best practices, and the requirements of the Commonwealth's new information security standard, SEC501-01, which will supersede the current standard on July 1, 2007.

Institute Inventory Controls for Community Resource Pharmacy

After two years of operations, the Community Resource Pharmacy does not have an automated inventory system. The pharmacy management states that they do not have the time or human resources necessary to institute and automated inventory system for pharmaceuticals.

In the summer of 2005, the Department reorganized its Hiram Davis Medical Center pharmacy operations into two physically separate pharmacies. While both pharmacies are still located within the basement of the medical center, one pharmacy provides medication exclusively to the Petersburg campus, and the second pharmacy, the Community Resource Pharmacy, provides medications to all Community Service Boards. Prior to the reorganization, the Department's Internal Audit Division reviewed the operations of the then AfterCare Pharmacy and provided their recommendations to management.

We concur with the findings of internal audit and recommend that the Department work to establish an automated inventory module for its pharmacies. An automated system should provide management with the necessary tools to manage and control its pharmaceutical costs effectively.

Strengthen Controls over Capital Asset Useful Life

The Department does not have proper controls in place for assigning and reevaluating useful lives of depreciable capital assets (buildings, equipment, and infrastructure). The Department has not developed and implemented an agency-specific useful life methodology. As a result, the Department has a significant amount of fully depreciated assets and that amount has steadily increased from $104 million in fiscal year 2002 to $125 million in fiscal year 2006; a significant portion being equipment assets.

Without an agency-specific methodology, and by not reevaluating the useful lives of current depreciable capital assets, the Department is not complying with the Governmental Accounting Standards

Board (GASB) Statement No. 34 or topic No. 30605 of the Commonwealth Accounting Policies and Procedures (CAPP) manual.

The Department should develop, document, and implement a methodology for assigning useful lives to depreciable capital assets and reevaluate currently assigned useful lives.

AGENCY HIGHLIGHTS

The Department of Mental Health, Mental Retardation, and Substance Abuse Services (Department) provides a wide array of services to individuals in 16 state-operated facilities, and in communities throughout the Commonwealth of Virginia. The Department has a central office that provides oversight for the 16 facilities. The facilities provide most of their own administrative functions and provide all direct services to the Department's consumers. In addition, the Department indirectly provides services through its funding and monitoring of 40 local Community Service Boards (Boards).

Central Office

The central office has direct responsibility for the programmatic, financial, and administrative operations of the state facilities. It also has responsibility for monitoring and overseeing the programmatic and financial activities of the Boards. In fiscal year 2006, the operations of the central office accounted for $38.8 million (6.4 percent) of the Department's total expenses.

The central office provides overall management and direction to the facilities. This includes developing an overall budget, financial management policies, and Medicare and Medicaid cost reports and reimbursement rates. They also provide internal audits, perform architectural and engineering services, administer capital outlay projects, and manage the information systems. Further, the central office provides technical assistance on human resource issues to the facilities and licenses all providers of mental health, mental retardation, and substance abuse services throughout the state. The Office of Inspector General, housed within the central office, independently investigates and monitors human rights issues at the facilities.

The central office bills and collects third party reimbursements, such as Medicaid and Medicare, through its field reimbursement offices located at various facilities. During fiscal year 2004, the central office implemented a new billing system, AVATAR, to meet HIPAA coding requirements for electronic health care transactions. Due to system implementation issues, electronic claims processing was not fully available until April 2005. A majority of the reimbursement offices delayed their billings until they could process their claims electronically, while other offices manually billed their claims.

The backlog of bills contributed to a 19 percent increase in the percentage of past due receivables between June 30, 2003 and June 30, 2004, as reflected in the table below. While total receivables have decreased since the system became operational, past due receivables have remained high because edit checks at the Department of Medical Assistance Services (Medical Assistance Services) rejected a number of Medicaid claims. The Department is currently working with Medical Assistance Services and reviewing individual accounts to clear these receivables. Management expects past due receivables to return to a normal level before the end of fiscal year 2007.

Department's Total Gross Receivable

Receivables:	June 30, 2003	June 30, 2004	June 30, 2005	June 30, 2006
Current (up to 60 days)	$52,164,582	$35,200,610	$36,596,813	$36,990,303
Past due (over 61 days)	4,157,419	12,600,615	10,402,870	8,819,710
Total	$56,322,001	$47,801,225	$46,999,683	$45,810,013
Percentage past due	7%	26 %	22%	19%

Medicare Part D Implementation

Medicare Part D (Part D), which went into effect January 1, 2006, subsidizes the costs of prescription drugs for Medicare beneficiaries. Prior to Part D, Medicaid subsidized the prescription costs of most individuals in state facilities. Approximately 50 percent of individuals in state facilities qualified for Part D benefits. Since these individuals still receive their medication from facility pharmacies, overall pharmaceutical costs have remained level. However, Part D shifted the reimbursement of pharmaceutical costs from Medicaid (state and federally funded) to Medicare (federally funded).

Unlike the facilities' pharmacies, the Community Resources Pharmacy (Resource Pharmacy), now under the central office, experienced a significant decrease in its overall pharmaceutical costs. The decrease resulted from the Boards diverting all Part D eligible individuals to private local pharmacies. Before the implementation of Medicare Part D, the Resource Pharmacy provided medications to approximately 17,000 individuals. Since the implementation of Part D, the pharmacy's client population has decreased by 53 percent, to about 8,000 individuals.

System Transformation Initiative

The central office has been working with both the facilities and the Boards as part of the state's System Transformation Initiative (Initiative). Part of the Initiative calls for Western State Hospital in Staunton, Eastern State Hospital in Williamsburg, Central Virginia Training Center in Lynchburg and Southeastern Virginia Training Center in Chesapeake to undergo major construction projects, which the Central Office will manage. The Department expects either the Virginia Public Building Authority or the Public Private Partnership Educational Facilities and Infrastructure Act of 2002 to finance the cost of facility replacements. The estimated replacement costs represented about $290 million of the Initiative.

The table below reflects the construction projects related to the Initiative.

Facility	Location	Current Bed Capacity	Fiscal Year 2006 Average Daily Census	Planned Bed Capacity	Funding Source	Funding Approved (Millions)	Amount Spent as of 2/6/07
Eastern State Hospital	Williamsburg						
Phase I - Hancock Geriatric Treatment Center		210	177	150	Bond	$22	$3,003,177
Phase II - Adult Mental Health Center		262	242	150	General Funds	59	-
Western State Hospital	Staunton	254	243	246	General Funds	2.5*	-
Central Virginia Training Center	Lynchburg	611	540	300	General Funds	2.5*	396,303
Southeastern Virginia Training Center	Chesapeake	200	189	100	General Funds	2.5*	279,651

* Planning only

Additionally, during fiscal 2006, Medical Assistance Services obtained an additional 145 mental retardation Home and Community-Based Waiver slots for the Department. These slots serve individuals on the statewide urgent needs list. The Department added another 110 waiver slots for children under the age of six. Additionally, the Department added 80 waiver slots for the Boards to manage. The Boards will focus these slots to address those patients affected by the rebuilding of the aforementioned state facilities.

Facilities

Sixteen facilities provide inpatient consumer care to over 3,000 individuals. Ten mental health facilities, referred to as "hospitals," provide acute care and chronic psychiatric services to children, adults, and the elderly. There are also five mental retardation facilities, referred to as "training centers," that offer residential care and training in such areas as language, self-care, independent living, academic skills, and motor development. Finally, the Virginia Center for Behavioral Rehabilitation houses convicted sex offenders who are civilly committed at the end of their prison sentence if the Department of Corrections deems them "sexually violent predators."

The following tables summarize each hospital's and training center's revenues, expenses, and populations for fiscal year 2006.

COMPARISON OF FACILITY OPERATIONS
Fiscal Year 2006
Hospital Facilities

	Central State Hospital	Eastern State Hospital	Southwestern Virginia Mental Health Institute	Western State Hospital
Average resident census	240	419	149	243
Total resident days	87,600	152,935	54,385	88,695
Revenue:				
Adjusted General Fund appropriations	$ 44,034,755	$ 45,960,876	$ 23,213,399	$ 44,080,558
Collections (third party reimbursements)	380,033	24,005,282	7,671,159	3,489,599
Collections for General Fund of the Commonwealth	28,356	5,451	-	14,084
Other revenues	28,048	14,468	-	3,715
Total revenue	44,471,191	69,986,077	30,884,558	47,587,956
Expenses:				
Personal services	38,497,045	54,832,706	25,439,354	39,063,533
Contractual services	5,331,294	2,730,998	2,845,046	2,952,882
Supplies and materials	771,530	7,890,637	3,371,311	4,560,501
Transfer payments	112,269	59,602	11,664	18,893
Insurance, rentals, and utilities	1,192,318	4,404,224	1,260,789	1,654,571
Property, plant, and equipment	550,229	346,647	196,972	530,066
Total expenses	$ 46,454,685	$ 70,264,814	$ 33,125,136	$ 48,780,448
Excess/(deficiency) of revenues over expenses	$ (1,983,494)	$ (278,737)	$ (2,240,578)	$ (1,192,491)
Expenses per resident	$ 193,561	$ 167,696	$ 222,316	$ 200,743
Expenses per resident day	$ 530	$ 459	$ 609	$ 550
Revenues per resident	$ 185,297	$ 167,031	$ 207,279	$ 195,835
Revenues per resident day	$ 508	$ 458	$ 568	$ 537

Commonwealth Center for Children & Adolescents	Catawba Hospital	Northern Virginia Mental Health Institute	Piedmont Geriatric Hospital	Southern Virginia Mental Health Institute	Hiram Davis Medical Center	Total for Mental Health Facilities
31	102	120	119	68	62	1,553
11,315	37,230	43,800	43,435	24,820	22,630	566,845
$ 6,685,278	$ 8,113,491	$ 24,671,590	$ 3,742,699	$ 10,665,573	$ 24,357,614	$ 235,525,833
1,925,554	8,771,917	1,652,979	16,861,331	2,379,533	14,358,923	81,496,309
27	40,793	1,250	-	-	4,601	94,561
-	1,505	1,037	231	-	-	49,004
8,610,859	16,927,706	26,326,856	20,604,261	13,045,106	38,721,138	317,165,707
7,640,066	15,388,223	19,610,179	16,382,580	9,184,523	9,493,083	235,531,294
395,161	1,892,565	2,941,233	1,300,137	1,206,486	1,776,992	23,372,794
555,638	1,826,343	2,429,367	1,950,671	964,870	27,086,558	51,407,425
3,587	11,177	30,072	10,690	4,987	2,133	265,075
403,619	547,176	638,693	549,726	406,502	142,387	11,200,005
86,709	80,123	218,052	313,999	149,275	55,653	2,527,726
$ 9,084,780	$ 19,745,607	$ 25,867,596	$ 20,507,803	$ 11,916,645	$ 38,556,806	$ 324,304,319
$ (473,921)	$ (2,817,901)	$ 459,260	$ 96,458	$ 1,128,461	$ 164,332	$ (7,138,611)
$ 293,057	$ 193,584	$ 215,563	$ 172,334	$ 175,245	$ 621,884	$ 208,824
$ 803	$ 530	$ 591	$ 472	$ 480	$ 1,704	$ 572
$ 277,770	$ 165,958	$ 219,390	$ 173,145	$ 191,840	$ 624,534	$ 204,228
$ 761	$ 455	$ 601	$ 474	$ 526	$ 1,711	$ 560

COMPARISON OF FACILITY OPERATIONS
Fiscal Year 2006
Training Centers

	Central Virginia Training Center	Southeastern Virginia Training Center
Average daily resident census	540	189
Total resident days (average daily resident census * 365 days)	197,100	68,985
Revenue:		
Adjusted General Fund appropriations	$ 9,353,089	$ 3,333,481
Collections (third party reimbursements) Fund 200	79,523,980	20,432,777
Collections for General Fund of the Commonwealth Fund 100	3,134	-
Other revenues	24,702	2,370
Total revenue	88,904,905	23,768,628
Expenses:		
Personal services	67,649,976	18,719,358
Contractual services	2,221,071	1,599,056
Supplies and materials	8,817,527	1,459,943
Transfer payments	-	44,463
Insurance, rentals, and utilities	2,961,063	975,904
Property, plant, and equipment	155,030	219,627
Total expenses	$ 81,804,667	$ 23,018,350
Excess/(deficiency) of revenue over expenses	$ 7,100,238	$ 750,278
Expenses per resident	$ 151,490	$ 121,790
Expenses per resident day	$ 415	$ 334
Revenues per resident	$ 164,639	$ 125,760
Revenues per resident day	$ 451	$ 345

Northern Virginia Training Center	Southside Virginia Training Center	Southwestern Virginia Training Center	Total for Retardation Training Centers
176	336	211	1,452
64,240	122,640	77,015	529,980
$ 5,049,137	$ 17,586,116	$ 2,758,271	$ 38,080,094
31,564,495	59,244,610	18,959,903	209,725,764
-	2,258	-	5,391
200	92,960	1,043	121,275
36,613,832	76,925,944	21,719,216	247,932,524
27,193,739	55,458,128	18,386,374	187,407,575
1,657,846	4,265,231	579,639	10,322,844
2,832,856	7,242,361	1,161,043	21,513,730
32,393	68,475	96,720	242,050
728,639	2,634,753	1,277,536	8,577,895
235,597	1,200,005	177,784	1,988,042
$ 32,681,070	$ 70,868,952	$ 21,679,097	$ 230,052,136
$ 3,932,761	$ 6,056,992	$ 40,120	$ 17,880,388
$ 185,688	$ 210,920	$ 102,745	$ 158,438
$ 509	$ 578	$ 281	$ 434
$ 208,033	$ 228,946	$ 102,935	$ 170,752
$ 570	$ 627	$ 282	$ 468

Comparison of Facility Operations

The tables show that per diem expenses range from $281 to $1,704 with an average per diem of $434 for training facilities and $572 for hospitals. Hiram Davis Medical Center accounts for the highest per diem cost due to the severe nature of its patients' both physical as well as psychiatric conditions and the pharmacy services that it provides to clients outside of its facility.

Overall, personal services are the facilities' largest expense, which is consistent with prior years, although in fiscal year 2006 the facilities incurred additional payroll cost in June 2006 due to the administration's response to a budget action. In fiscal year 2006, the training facilities and hospitals spent over $422 million, or 76 percent, of their total expenses on personal services.

The facilities' largest source of revenue is collections from third-party payers, primarily Medicaid. In fiscal year 2006, these third-party payers accounted for approximately 52 percent of the facilities' total available resources, or roughly $291 million.

The Appropriation Act show collected Medicaid and Medicare fees as special revenue and amounts are appropriated by facility. However, the central office can request transfers of special revenues among the individual facilities to cover other facilities' cost where expenses exceed revenues. Since each facility receives both General and Special Revenue funding and the mental health facilities do not usually generate sufficient revenues to cover expenses, the central office closely monitors the income and expenses of each facility.

When it is apparent that the mental retardation facilities will generate sufficient revenues to cover their expenses, the central office transfers the excess collections to cover the shortfall in other mental health facilities. This practice allows the Department to operate all of its facilities within its overall appropriation.

This budgetary method may have long-term critical consequences, as the federal government enacts changes to their Medicaid reimbursement policies. Additionally, this practice also tends to show a more even distribution of General Fund appropriations among all facilities, when in reality, the transfer of special fund revenue indicates that some mental retardation units could operate more independently, and other mental health facilities would need additional General Fund appropriations. The Department is working to reduce the amount of needed budgetary transfers and as a result, has decreased the amount of transfers compared to prior years, as seen in the next table.

The table below provides a detailed analysis of transfer payments in fiscal year 2006 for each facility with summary figures for comparison purposes for fiscal years 2004, 2005, and 2006.

Fiscal Year 2006 Special Revenue Comparison

Facility	Original Appropriation	Adjusted Budget	Revenues Collected	Transfers In/(Out)	Expenses
Catawba State Hospital	$ 9,992,307	$ 11,632,673	$ 8,771,917	$ 2,990,603	$ 11,632,116
Central State Hospital	2,428,072	2,428,072	408,081	2,086,433	2,428,010
Comm. Ctr. For Children & Adolescents	2,019,682	2,351,609	1,925,554	1,000,000	2,347,388
Eastern State Hospital	21,974,024	25,379,867	24,007,572	(1,278,800)	24,303,939
Hiram W. Davis Medical Center	11,283,142	13,822,684	14,358,923	(1,800,000)	13,822,679
Northern Virginia Mental Health Institute	1,172,475	1,197,068	1,652,979	(500,000)	1,197,067
Piedmont Geriatric Hospital	15,778,184	16,765,104	16,861,331	750,000	16,765,104
Southern Virginia Mental Health Institute	1,376,236	1,376,236	2,379,533	(750,000)	1,251,236
Southwestern Va. Mental Health Institute	7,818,507	9,891,820	7,677,881	1,600,000	9,891,820
Western State Hospital	4,147,852	4,768,649	3,489,599	1,450,000	4,698,961
2006 Total	$ 77,990,481	$ 89,613,782	$ 81,533,369	$ 5,548,236	$ 88,338,319
2005 Total	$ 77,990,481	$ 81,224,844	$ 75,279,549	$12,056,972	$ 81,343,914
2004 Total	$ 87,984,164	$ 89,036,129	$ 74,023,396	$15,855,000	$ 89,133,274
Central Virginia Training Center	$ 66,365,586	$ 72,466,315	$ 79,543,802	($4,750,000)	$ 72,451,934
Northern Virginia Training Center	25,590,971	27,632,495	31,654,495	(1,500,000)	27,631,935
Southeastern Virginia Training Center	16,511,636	19,670,491	20,432,777	1,500,000	19,670,461
Southside Virginia Training Center	50,787,805	$53,085,323	59,336,370	(4,059,123)	53,066,873
Southwestern Virginia Training Center	16,727,99	18,897,435	18,960,791	500,000	18,893,478
2006 Total	$ 175,983,994	$ 191,752,059	$ 209,928,235	($8,309,123)	$191,714,681
2005 Total	$ 175,983,994	$ 179,462,936	$ 195,228,788	($14,413,431)	$179,438,723
2004 Total	$173,619,858	$ 173,459,336	$ 192,784,290	($20,229,629)	$173,430,545

Virginia Center for Behavioral Rehabilitation

The Virginia Center for Behavioral Rehabilitation (Center) opened in October 2003 in response to an immediate need to accommodate individuals who would be civilly committed as sexually violent predators following their criminal sentences. The state needed a facility to provide individualized rehabilitation services in a secure environment. The immediacy of the need resulted in the Department retrofitting an existing building on their Petersburg complex to accommodate an operating capacity of 36. The average daily census was 11 in fiscal 2005 and 28 in fiscal 2006.

The table below shows the high Per Diem cost of the current facility, caused by a small patient population and the large number of employees needed to both operate the center and achieve appropriate security levels and program effectiveness.

COMPARISON OF FACILITY OPERATIONS
Fiscal Year 2006
Behavioral Rehabilitation Facility

	Virginia Center for Behavioral Rehabilitation
Average resident census	28
Total resident days	10220
Revenue:	
Adjusted General Fund appropriations	$ 5,397,523
Fund 100-General Fund, other revenue	-
Fund 600-Internal Service Fund, sales of property and commodities	-
Total revenue	5,397,523
Expenses:	
Personal services	3,980,650
Contractual services	682,926
Supplies and materials	289,313
Transfer payments	7,696
Insurance, rentals, and utilities	78,001
Property, plant, and equipment	357,934
Total expenses	$ 5,396,519
Excess/(deficiency) of revenues over expenses	$ 1,004
Expenses per resident	$ 192,733
Expenses per resident day	$ 528
Revenues per resident	$ 192,769
Revenues per resident day	$ 528

The Center's occupancy will increase dramatically based upon an imposed change in the screening criteria for facility placement. The Department is currently overseeing the construction of a $62 million, 300-bed facility in Nottoway County. As of February 2007, construction expenses amounted to approximately $45.4 million. Management expects to open the new center in February 2008.

Community Service Boards

Community Service Boards (Boards) are the single point of entry into the Commonwealth's Mental Health, Mental Retardation, and Substance Abuse Services system, which includes providing access to state mental health and mental retardation facilities, as well as community programs. Individuals who seek services from a Board receive an intake evaluation to determine the type and duration of services needed. The Boards provide pre-admission screening and discharge planning services for consumers entering or leaving state facilities.

In addition, the Boards function as providers of services (directly or contractually), advisors to their local government, client advocates, community educators, and planners on issues related to mental health, mental retardation, and substance abuse. In contrast to hospitalization, the Boards provide services by drawing on community resources and support systems, such as the family and friends of patients. During fiscal year 2006, the Department transferred $241 million (28.7 percent of its total budget) to the Boards.

The Boards access medications for eligible consumers through the Community Resource Pharmacy, located within the Hiram Davis Medical Center in Petersburg. They provide medications for individuals who have been discharged or diverted from state facilities and have Medicaid or cannot pay for medications to treat or prevent a recurrence of their condition. Each year, the Department provides the Boards with a capped amount of state-funded medication. The Department bases these amounts on the historical costs of covering prescription drugs for those individuals who are unable to pay. The Boards direct individuals eligible for Medicare Part D benefits to outside pharmacies.

Initiatives in the public Mental Health, Mental Retardation, and Substance Abuse Services industry stress the benefits of community-based care for this population of citizens. As these initiatives reduce state facility capacity and increase demand on community services, the Department's ongoing and collaborative efforts with Boards and other stakeholders is vital to the success of the transformation.

The Department monitors this transformation through various implementation committees. The Facility Capital Replacement Project has the responsibility of coordinating the planning for each of the state facility projects. In addition, the Department will ensure that the transformation from state facilities to community-based care is effective and efficient by using the following committees:

- Service Development Group: The Service Development Group is responsible for coordinating the development of regional and Board-specific plans, and for the implementation of these plans.

- Training and Education Committee: The Training and Education Committee is responsible for developing a program of peer and project providers.

- Data Outcome Measures Group: The Data Outcome Measures Group is responsible for coordinating the development of outcome measures and the identification of the data.

Commonwealth of Virginia

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June 14, 2007

The Honorable Timothy M. Kaine
Governor of Virginia
State Capital
Richmond, Virginia

The Honorable Thomas K. Norment, Jr.
Chairman, Joint Legislative Audit
and Review Commission
General Assembly Building
Richmond, Virginia

We have audited the financial records and operations of the **Department of Mental Health, Mental Retardation and Substance Abuse Services** (Department) for the year ended June 30 2006. We conducted our audit in accordance with Government Auditing Standards, issued by the Comptroller General of the United States.

Audit Objectives

Our audit's primary objective was to evaluate the accuracy of the Department's financial transactions as reported in the Comprehensive Annual Financial Report for the Commonwealth of Virginia for the year ended June 30, 2006 and test compliance for the Statewide Single Audit. In support of this objective, we evaluated the accuracy of recording financial transactions on the Commonwealth Accounting and Reporting System and in the Department's accounting records, reviewed the adequacy of the Department's internal control, tested for compliance with applicable laws, regulations, contracts, and grant agreements, and reviewed corrective actions of audit findings from prior year reports.

Audit Scope and Methodology

The Department's management has responsibility for establishing and maintaining internal control and complying with applicable laws and regulations. Internal control is a process designed to provide reasonable, but not absolute, assurance regarding the reliability of financial reporting, effectiveness and efficiency of operations, and compliance with applicable laws and regulations.

We gained an understanding of the overall internal controls, both automated and manual, sufficient to plan the audit. We considered materiality and control risk in determining the nature and extent of our audit procedures. Our review encompassed controls over the following significant cycles, classes of transactions, and account balances.

Payroll expenses
Federal grant revenues and expenses
Contractual services expenses
Appropriations
Collections and accounts receivable
Community Resource Pharmacy
Capital assets
Network security

We performed audit tests to determine whether the Department's controls were adequate, had been placed in operation, and were being followed. Our audit also included tests of compliance with provisions of applicable laws and regulations. Our audit procedures included inquiries of appropriate personnel, inspection of documents, records, and contracts, and observation of the Department's operations. We tested transactions and performed analytical procedures, including budgetary and trend analyses.

Conclusions

We found that the Department properly stated, in all material respects, the amounts recorded and reported in the Commonwealth Accounting and Reporting System. The Department's records its financial transactions on the cash basis of accounting, which is a comprehensive basis of accounting other than accounting principles generally accepted in the United States of America. The financial information presented in this report came directly from the Commonwealth Accounting and Reporting System.

We noted certain matters involving internal control and its operation and compliance with applicable laws and regulations that require management's attention and corrective action. These matters are described in the section entitled "Audit Findings and Recommendations."

The Department has taken adequate corrective action with respect to audit findings reported in the prior year.

EXIT CONFERENCE AND REPORT DISTRIBUTION

We discussed this report with management on June 14, 2007. Management's response has been included at the end of this report.

This report is intended for the information and use of the Governor and General Assembly, management, and the citizens of the Commonwealth of Virginia and is a public record.

AUDITOR OF PUBLIC ACCOUNTS

GDS/sks

COMMONWEALTH of VIRGINIA

DEPARTMENT OF
MENTAL HEALTH, MENTAL RETARDATION AND SUBSTANCE ABUSE SERVICES

JAMES S. REINHARD, M.D.
COMMISSIONER

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June 27, 2007

Mr. Walt Kucharski
Auditor of Public Accounts
101 North 14th Street
Monroe Building, 8th Floor
Richmond, Virginia 23219

Dear Mr. Kucharski:

Presented below are our responses to the fiscal year 2006 audit report for DMHMRSAS.

Strengthen Monitoring of Community Services Boards

There are numerous monitoring procedures used by the Department to oversee CSB operations. These are included in a matrix of oversight responsibilities maintained by the Office of Community Services Administration. We have not fully documented all of our monitoring procedures but are in the process of doing so. Each office responsible for sub-recipient monitoring is submitting its procedures to the Office of Budget and Financial Reporting where they will be consolidated and a written set of procedures produced.

Expand Security Awareness Training Program

DMHMRSAS has developed this training program and it will be in place by the July 1, 2007 date established by the Commonwealth's information security standard.

Obtain Security Risk Assurance for Infrastructure

We agree with this finding. Please be aware that this finding and recommendation has much to do with VITA and is not completely under the control of DMHMRSAS.

Institute Inventory Controls for Community Resource Pharmacy

We concur that there is no automated inventory system in place at the community resource pharmacy. A pharmacy module is being developed as part of the electronic health records project beginning in FY 2008.

Strengthen Controls Over Capital Asset Useful Life

As was discussed in the exit conference, this comment is common to most if not all state agencies. We agree and will develop a procedure in order to be in compliance with GASB 34 reporting standards.

General Comments

In the second paragraph of the "Comparison of Facility Operations" portion of the report it is important to note the fact that there was a 25th pay period in FY 2006 due to the General Assembly going past its deadline. The Appropriations Act that year was actually dated June 30, 2006 so we barely averted a closure of operations going into this current biennium. This was the reason for the 25th payroll in fiscal year 2006.

In the sixth paragraph of the "Comparison of Facility Operations" portion of the report it is stated that we make cash transfers across various facilities. If our General Fund match at DMAS were adequate so as to allow us to generate our true Medicaid revenues each fiscal year, we would have virtually no need for any cash transfers during the year. Because this amount is less than our ability to generate Medicaid revenues, we are forced to transfer General Fund appropriation to DMAS to increase our match. Because MH facilities are appropriated majority GF funding and because this is what we transfer to DMAS, the GF appropriation transferred is replaced by Special Fund appropriation. This must be backed by cash. In order to back the appropriation we must transfer cash from MR facilities to MH facilities.
Without an outside fix for our match problem we have no choice but to operate in this manner.

I trust that this response meets your needs. Should you have further questions please do not hesitate to contact me.

Sincerely,

Joy Yeh, Assistant Commissioner
Finance and Administration

Cc: James Reinhard
Ray Ratke
Frank Tetrick
Jerry Deans
Paul Gilding
Ken Gunn
Rosanna Roberts
John Jackson

AGENCY OFFICIALS

THE DEPARTMENT OF MENTAL HEALTH, MENTAL RETARDATION, AND SUBSTANCE ABUSE SERVICES

James Reinhard, M.D., Commissioner

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