STATE OF NORTH CAROLINA

FISCAL CONTROL AUDIT REPORT ON

DEPARTMENT OF HEALTH AND HUMAN SERVICES

DIVISION OF MENTAL HEALTH, DEVELOPMENTAL DISABILITIES AND SUBSTANCE ABUSE SERVICES

CHERRY HOSPITAL

GOLDSBORO, NORTH CAROLINA

FOR THE PERIOD JULY 1, 2004, THROUGH JANUARY 31, 2005

OFFICE OF THE STATE AUDITOR

LESLIE W. MERRITT, JR., CPA, CFP

STATE AUDITOR

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Ms. Carmen Hooker Odom, Secretary,
Department of Health and Human Services
Mr. Michael Moseley, Director, Division of Mental Health,
Developmental Disabilities and Substance Abuse Services
Dr. James Osberg, Interim Director, Cherry Hospital

This report presents the results of our fiscal control audit of Cherry Hospital for the period July 1, 2004, through January 31, 2005. Our work was performed by authority of Article 5A of Chapter 147 of the *North Carolina General Statutes* and was conducted in accordance with the standards contained in *Government Auditing Standards* issued by the Comptroller General of the United States. The objective of a fiscal control audit is to gather and evaluate evidence about internal control over selected fiscal matters, such as financial accounting and reporting; compliance with finance-related laws, regulations, and provisions of contracts or grant agreements; and/or management of financial resources.

The results of our audit disclosed deficiencies in internal control and/or instances of noncompliance or other matters that are considered reportable under *Government Auditing Standards*. These items are described in the Audit Findings and Recommendations section of this report.

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Leslie W. Merritt, Jr.

Leslie W. Merritt, Jr., CPA, CFP
State Auditor

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BACKGROUND INFORMATION

Cherry Hospital, located in Goldsboro, North Carolina, is an accredited state funded psychiatric hospital serving 33 counties in the eastern region of North Carolina. It provides inpatient psychiatric services to individuals in need of such services who are age 13 and above. Its patients come from a variety of cultural backgrounds with the majority being indigent or slightly above the poverty level. The average daily census is approximately 300 patients.

The Hospital charges the patient based upon the patient's ability to pay, but no one is refused treatment because of inability to pay. Cherry Hospital has an annual operating budget of approximately $66 million. The most significant operating cost is salaries and benefits for hospital employees. There are 1,183 positions available with approximately 950 filled. The Hospital also uses nurses that are contracted from private vendors. Other major expenditure accounts include drugs and other pharmacy supplies.

Management at Cherry Hospital reports to the Division of Mental Health, Developmental Disabilities and Substance Abuse Services. The Division is part of the Department of Health and Human Services.

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OBJECTIVES, SCOPE, METHODOLOGY, AND RESULTS

OBJECTIVES

As authorized by Article 5A of Chapter 147 of the *North Carolina General Statutes* and in accordance with the standards contained in *Government Auditing Standards* issued by the Comptroller General of the United States, we have conducted a fiscal control audit at Cherry Hospital.

The objective of a fiscal control audit is to gather and evaluate evidence about internal control over selected fiscal matters, such as financial accounting and reporting; compliance with finance-related laws, regulations, and provisions of contracts or grant agreements; and/or management of financial resources. Our audit does not provide a basis for issuing an opinion on internal control, and consequently, we have not issued such an opinion.

Management is responsible for establishing and maintaining effective internal control. Internal control is a process designed to provide reasonable assurance that relevant objectives are achieved. Because of inherent limitations in internal control, errors or fraud may nevertheless occur and not be detected. Also, projections of any evaluation of internal control to future periods are subject to the risk that conditions may change or compliance with policies and procedures may deteriorate.

SCOPE

Our audit scope covered the period of July 1, 2004, through January 31, 2005, and included selected internal controls from the following accounts:

Payroll Expenditures – We reviewed regular, overtime, extended duty, call/back and shift premium pay for hospital employees. Overtime is paid to employees subject to wage and hour laws who work more than 40 hours a week. Doctors receive extended duty pay if their work hours exceed 40 hours a week. Doctors and some maintenance personnel receive call/back pay if they return to work outside of their regular work schedule. Shift premium is paid when employees work during hours other than traditional business hours. We examined internal controls to ensure that payroll expenditures were properly accounted for and that payments complied with the State's and the Hospital's personnel and timekeeping policies. In addition, we tested the Hospital's control and management of overtime pay. The Hospital paid $28.8 million in employee salaries during the seven-month audit period of which $1.8 million was for overtime.

Inventory Procedures – We reviewed internal controls over the drugs, medical supplies, and vehicles inventory accounts. The hospital pharmacy dispensed $1.5 million in drugs during the seven-month audit period. The staff includes eight pharmacists and four pharmacy technicians. Also, a central services section exists to provide storage, distribution, and accountability of medical supplies for patient use.

Operating/Petty Cash – The cashier's office is the centralized receipting unit for the Hospital. We reviewed internal controls over daily balancing procedures.

METHODOLOGY

To accomplish our audit objectives, we gained an understanding of internal control, performed tests of control effectiveness, and/or performed direct tests of the accounts and transactions as we considered necessary in the circumstances. Specifically, we performed procedures such as interviewing personnel, observing operations, reviewing policies, analyzing accounting records and examining documentation supporting recorded transactions and balances.

RESULTS

The results of our audit disclosed deficiencies in internal control and/or instances of noncompliance that are considered reportable under *Government Auditing Standards*. These items are described in the Audit Findings and Recommendations section of this report.

AUDIT FINDINGS AND RECOMMENDATIONS

1. MANAGEMENT OF OVERTIME IS NOT EFFECTIVE

Management does not have effective policies governing the scheduling of overtime, has not adequately monitored overtime, and has not adequately provided back-up resources to meet the Hospital's staffing needs. Patient-care staff frequently worked overtime without the nurse manager's knowledge by volunteering and working for patient-care units other than the ones to which they were assigned. Excessive overtime causes employee exhaustion and could adversely affect patient care.

During the seven-month audit period, 51 patient-care employees worked overtime in excess of 90 hours at least one month. Nine of these employees worked in excess of 90 hours a month for at least four months in the audit period. Twelve of these employees worked overtime ranging from 150 hours to as many as 260 hours overtime in a single month. One employee worked overtime every month of the audit period, with overtime alone ranging from 164 to 260 hours per month.

Recommendation: Overtime polices and procedures should be clearly documented and practices should be monitored to ensure that resources are used efficiently, effectively and not to the detriment of patients. Overtime should be reviewed and approved in advance by the appropriate staff.

Agency Response:

Recommendation: Overtime policies and procedures should be clearly documented and practices should be monitored to ensure that resources are used efficiently, effectively, and not to the detriment of patients.

DHHS Response: The Department agrees with the finding and recommendation. A number of factors impacted the significant number of hours of overtime worked and paid during the audit period. These included:

- Cherry hired few HCTs from July, 2003 through October, 2004 in order to have vacant positions to revert to meet budget reduction goals for downsizing which was then in-process. In late 2004, management determined to meet downsizing budget goals with other funds, thus freeing 32 HCT positions for recruitment. These new hires began working in patient care units in January, 2005.
- From July 1, 2004 through January 31, 2005, 21 HCTs were on family medical leave or Worker's Compensation.
- From July 1, 2004 through January 31, 2005, 35 HCTs resigned, retired, or were dismissed, reducing the pool of available workers.

- From July 1, 2004 through January 31, 2005, 36 RNs/LPNs resigned, retired or were dismissed.
- From July 1, 2004 through January 31, 2005, ten RNs/LPNs were on family medical leave or Workers Compensation.

To reduce overtime, the following steps have been implemented:

- 20 additional HCT positions are in process of being recruited which will reduce demand for overtime.
- RNs/LPNs are continuously recruited by a full-time recruiter in the Cherry Hospital Nursing Office.

In addition, in January 2005 the Nursing Department began the implementation of new procedures to reduce overtime which included:

- Nurse Managers were re-educated regarding their responsibility to develop monthly employee time schedules which did not create overtime. Education focused on planning the monthly schedule to ensure that their unit based staff resources were balanced across all three shifts and on weekends.
- Scheduling strategies which could minimize overtime were evaluated. This included staff reassignments to other buildings based on patient need, shift/weekend reassignments, and alterations in special scheduling options. All unit schedules were reviewed to validate that resources were being scheduled to meet the mandatory staffing levels required for each unit. Leave policies were reviewed to reinforce that managers should consider mandatory staffing requirements before automatically granting unscheduled leave time.
- A centralized approach to overtime authorization was implemented in February 2005. The practice of allowing each building to fill their overtime needs was discontinued as it was recognized that efficient use of the resources was not accomplished with each nursing unit independently filling their overtime needs. That is, one building may be scheduling staff to work overtime when there were available resources in another building on campus.
- A memo was sent to all employees outlining the procedures for the new centralized overtime system. The system shifted to all overtime being approved by the Royster Nursing Office on a shift-by-shift basis based on patient need. This allowed a more global perspective of resources that are available across campus. When there is an identified need for resources, the Royster Nursing Office Supervisor checks coverage available across campus, and reassigns staff if possible. Overtime is authorized only if the RNO Supervisor determines that the overtime request is justified and there are no other options available for coverage.
- The availability of temporary/part-time staff is also considered prior to authorizing overtime of full time staff.

- To monitor the overtime utilization, a spreadsheet was developed by the Royster Nursing Office. Prior to centralization of overtime, each building was signing up employees for overtime and there was no daily tracking mechanism to determine the amount of hours each employee worked. Since employees could volunteer in multiple buildings across campus, excessive amounts of overtime could be generated by one employee without their supervisor's knowledge. All overtime worked is entered into the data base on a shift-by-shift basis, creating a mechanism to monitor each employee's overtime hours. Before authorizing overtime, the data base is checked to determine that the employee has not exceeded the maximum of 24 hours of overtime per week.
- Controls were put in place in regard to the overtime forms. All overtime is documented on a form which is submitted directly to the Nursing Office. The Nursing Office validates the approval and stamps the form. The practice of allowing employees to submit the forms directly to the timekeeper without a supervisor's signature was discontinued.

Recommendation: Overtime should *be reviewed and approved in advance by the appropriate staff.*

DHHS Response: The Department agrees with this recommendation.

The Nursing Department has implemented processes which require authorization of all overtime on a shift-by-shift basis by a designated supervisor.

- All overtime is approved centrally through the Nursing Office. Coverage for all nursing units is evaluated each shift to determine how the nursing resources should be assigned. This is accomplished by a designated supervisor who compares the staffing requirements in each building and the resources available across campus. Staff resources are then deployed where needed.
- If staffing needs exist which cannot be covered by existing resources, overtime is authorized by the Nursing Office Supervisor. Communication occurs between the Nursing Office Supervisor and the individual building supervisor to validate any overtime that has been approved.
- There is a designated process in place for employees who wish to volunteer to work overtime. Requests to work overtime are matched with existing scheduling needs. Requests for overtime are approved only if there is a justified need. The requests for overtime are kept on file in the Nursing Office for reference throughout the month as coverage issues arise.

2. INVENTORY CONTROLS NEED IMPROVING

The Hospital's controls over certain types of inventory were deficient. Theft, concealment of shortages, spoilage, or unauthorized use can occur if adequate controls are not in place and could lead to inaccurate financial statements. Inventories that are not

managed properly can cause the accumulation of excessive stock. We noted the following deficiencies with regard to the pharmacy and medical supply inventories:

- Non-controlled substances, which comprise the majority of drugs purchased and dispensed by the Hospital, are not tracked in any type of perpetual inventory system, as are controlled substances, medical supplies, and other types of supplies;
- The Hospital's purchasing practices have resulted in stockpiling and the accumulation of excessive inventory. The Hospital's practice has generally been to maintain a five-month supply of medical supplies on hand;
- The perpetual inventory records for medical supplies were not recorded correctly. We found differences between quantities on hand and the perpetual inventory records for selected high-risk items. In addition, the ending inventory balance at June 30, 2004, was overstated by $10,668 because an adjustment for shortages was not posted. The shortage represented 28 percent of the recorded medical supply inventory.

The Department of Health and Human Services' *Cash Management Plan* states that inventory quantities should be at levels sufficient to conduct business without disruption. Good internal controls require that assets be properly safeguarded and accounted for.

Recommendation: The Hospital should implement a system to adequately account for non-controlled substances, which may include adding non-controlled substances to the perpetual inventory system. Inventories should be managed in a manner that ensures that only the minimum supply necessary is in stock. Adjustments to inventory should be properly and promptly recorded.

Agency Response:

Recommendation: The hospital should implement a system to adequately account for non-controlled substances, which may include adding non-controlled substances to the perpetual inventory.

DHHS Response: The Department agrees with this finding and recommendation.

The Pharmacy Department, through the hospital Pharmacy and Thera-peutics Committee, will sharply reduce the list of "ward stock" medications and issue these medications from Pharmacy on a per-patient basis. This will significantly reduce the inventory for these items and decrease the possibility of theft, spoilage, and unauthorized use. This action will be in effect by October 31, 2005.

By June 30, 2006, hospital management will explore the options available and the feasibility of implementing a perpetual inventory system for non-controlled substance medications.

Recommendation: Inventories should be managed in a manner that ensures that only the minimum supply necessary is in stock.

DHHS Response: The Department agrees with this recommendation.

Purchasing practices will be changed effective September 1, 2005 to maintain a 90 day supply of medical supplies on hand which will reduce stockpiling and the accumulation of excessive inventory. Effective September 1, 2005, responsibility for the Central Medical Supplies area will switch from the Pharmacy Department to the Cherry Hospital Warehouse Manager, who will be able to more closely monitor stocks of medical supplies. Limited access to the Central Medical Supply areas will be maintained for added security in this area.

Recommendation: Adjustments to inventory should be properly and promptly recorded.

The Department agrees with this recommendation. Effective September 1, 2005, inventory of medical stock will be done on a weekly basis to ensure that the inventory records for medical supplies are recorded correctly and adjustments to the inventory done in a timely manner. Also, the annual inventory for the fiscal year ending inventory will be adjusted for any shortages at June 30.

3. TIMEKEEPING CONTROLS NEED TO BE IMPROVED

Our examination of time documents for a sample of 60 employees indicated significant control deficiencies over timekeeping. Employees could be paid incorrectly when time and attendance is not properly documented and records are not reviewed and approved. There were at least six instances of each of the deficiencies listed below:

- Documentation such as timesheets, overtime requests, compensatory leave requests, extended duty documents were missing or not completed accurately;
- Supervisors did not approve timesheets or overtime/compensatory time requests;
- Timesheets and other time documentation did not agree with the recorded time and was not sufficient to determine if the employee was paid correctly.

In addition, other tests uncovered more deficiencies. We found instances where sick leave was recorded on the employee's timesheet, but not on the timekeeper's record. An employee was paid for a week for which the employee received worker's compensation. The overpayment was later recovered. Another employee reported taking 11 hours of compensatory leave in one day and another reported, in error, working 39 consecutive hours on extended duty. Also, timesheets were not submitted to the timekeepers on a weekly basis as required by policy. The tracking sheet for one of the four timekeepers indicated several missing timesheets that were already four days late.

Recommendation: The Hospital should review and modify procedures as necessary to ensure compliance with its payroll and personnel polices. The importance of following the hospital's polices and procedures should be communicated to the staff.

Agency Response:

Recommendation: Review and modify procedures as necessary to ensure compliance with payroll and personnel policies.

DHHS Response: The Department agrees with this finding and recommendation.

The following steps are designed to ensure compliance with payroll and personnel policies:

- Procedures (review by timekeepers and report back to staff supervisor) have been implemented to ensure that timesheets are signed by the employee and the supervisor. If overtime or compensatory time is earned, the Chief or Department Head also must sign the timesheet. Monthly timesheets (for salaried employees) must be turned in within 3 business days after the end of the month, and weekly timesheets must be turned in by Thursday following the work week ending on Tuesday.
- Procedures (timekeeper review) have been implemented to ensure that all required signatures are on the Overtime/Comp Time Tracking Form.
- A procedure has been established for communication among Human Resources, timekeeping, and Nursing Services when employees no longer have accrued leave to cover work absences. Cherry has established a committee to meet quarterly or more often if needed. The first meeting was August 8, 2005. The purpose of this committee is to collectively identify procedural best practices within the agency, conduct random audits, and identify supervisory training needs. In addition, this intentional dialogue will foster an environment of increased communication and structured meeting minutes which will be distributed to serve as a reference for supervisors. The members of this committee are the Budget Officer, Lead Time Keeper, Nursing Services Administrator, Salary Administrator, and Workers Compensation Administrator.
- Recognizing the volume of time keeping recordings for the Nursing Services unit and the need for a single source point of contact for this largely dispersed unit, the Hospital has identified the need for a clerical position. The primary purpose of this position is to serve as a liaison between time keeping and Nursing Services. This liaison will review, calculate, and process monthly overtime submittals, workers compensation leave, Family Medical Leave, and ensure timely submission of monthly and weekly time sheets, which will minimize and/or eliminate a number of the audit findings. The position is pending reclassification with an expected hire date of October 15, 2005.

4. ACCESS TO THE STATE'S PERSONNEL SYSTEM SHOULD BE REVOKED

Six hospital employees had access rights to the State Personnel System that they did not need. The access rights permitted some of the six to create and approve personnel-related forms. Inadequate security over systems may allow unauthorized persons to view and/or modify records.

Recommendation: Access controls to the State Personnel System should be strengthened. The Hospital should terminate user access to the State's computer systems in a timely manner for users no longer authorized and/or needing access. Periodic security access reviews should be conducted to ensure that access is restricted to users needing access.

Agency Response:

Recommendation: Access controls to the State Personnel System should be strengthened. The hospital should terminate user access in a timely manner for users no longer authorized and/or needing access.

DHHS Response: The Department agrees with this finding and recommendation.

During the audit period, all six employees identified as having "unauthorized" access to Cherry Hospital State Personnel System were entitled to have access due in part to being housed in the same facility while serving the Cherry O'Berry Alliance. Dual access was granted in an effort to maximize manpower by enabling the specialists to cross-train and work together as a team in the areas of Classification, Recruitment, Salary Administration, Workers' Compensation, Retirement, Position Control, and Employee Relations. These six employees were authorized to have access to the agencies they supported during the Alliance. This access allowed for each team of specialists to work jointly in accordance with the intent of the newly formed Alliance effective January 31, 2004.

Upon notification of the auditor's finding, Mr. Carmichael, Director of HR, immediately restricted this dual access and limited access to employees specifically assigned to each institution. Today, Mr. Carmichael is the only employee who continues to have dual access to both O'Berry Center and Cherry Hospital. Prior to the audit, Mr. Carmichael utilized Glenda Potts, Assistant HR Director for the Human Resource Department, to serve as his contact to address any HR issue for both institutions in his absence. Because Ms. Potts no longer has access to Cherry Hospital's PMIS, Mr. Carmichael now identifies two contact employees in his absence, one at each institution. In addressing the auditor's concerns to eliminate dual access to PMIS, our HR employees no longer have this resource to work as a team in serving both agencies, but instead function in two separate departments under the supervision of one shared Human Resource Director.

In addition, Cherry Hospital HIPAA Security Policy requires termination of network access for planned or unplanned employee absences of greater than 30 days.

Recommendation: Periodic security access reviews should be conducted to ensure that access is restricted to users needing access.

The Department agrees with this recommendation. As recommended by the Office of the State Auditor, Cherry Hospital has a mechanism in place to review security access for each employee who has a change in responsibility or separates from employment. The Division of Human Resources requires an annual review of this authorized access. In addition, Cherry Hospital has implemented a semi-annual review to ensure that access is restricted to users needing access.

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November 17, 2005

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