

State of Michigan

Department of Licensing and Regulatory Affairs Michigan Indigent Defense Commission Grant Management Phase 2 Consulting Report January 2022



Internal Audit Services
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STATE OF MICHIGAN
STATE BUDGET OFFICE
LANSING

CHRISTOPHER HARKINS
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January 5, 2022

Executive Summary

TO: Orlene Hawks, Director
Department of Licensing and Regulatory Affairs (LARA)

Christine A. Green, Chair
Michigan Indigent Defense Commission

FROM: Richard T. Lowe, Chief Internal Auditor *Richard T. Lowe*
Office of Internal Audit Services (OIAS)

Ed Brickner, Division Director *Edward J. Brickner*

SUBJECT: Consulting Engagement – Michigan Indigent Defense Commission Grant
Management Phase 2

This document contains our consulting report of the Michigan Indigent Defense Commission (MIDC) grant management processes Phase 2. In January of 2021, LARA asked OIAS to assist MIDC with improving its guidance to local indigent criminal defense systems (local systems) for managing financial oversight of subgrantees and to review allowability of expenses submitted for the MIDC grant program for the selected local system.

We determined that MIDC should enhance its guidance to local systems for monitoring their subgrantees. Additionally, we identified disallowed costs totaling \$87,616.

The following table displays our engagement conclusions, audit observations, and risk classifications. Please refer to Appendix A for more detail.

| | |
|---|---------------------------------------|
| Objective: To assist MIDC with improving its guidance to local systems for managing financial oversight of subgrantees, including nonprofit public defender offices, in compliance with PA 0214 of 2018 and other applicable policies and procedures, laws, regulations, and guidelines. | Conclusion: Improvement Needed |
| Observation: MIDC should update its grant agreement template to include nonprofit public defender offices under its definition of subgrantees. | Risk: Moderate |



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| <p>Observation: MIDC should enhance existing guidance to specify the monitoring activities local systems are required to perform to ensure subgrantees comply with the terms and conditions of the grant agreement.</p> | <p>Risk: Moderate</p> |
| <p>Objective: Review allowability of expenses submitted for the MIDC grant program for the selected local system.</p> | <p>Conclusion: Well Controlled with Opportunities for Improvement</p> |
| <p>Observation: Ensure local systems adequately monitor their vendors and subgrantees and enforce the requirement that local systems provide documentation to support their expenses.</p> | <p>Risk: Low</p> |

During our review, OIAS noted MIDC implemented the proactive measure of requiring local systems with subgrantees to provide copies of the subgrantees’ detailed budgets. MIDC staff members then reviewed the budgets to identify potentially ineligible expenses and follow up with the local systems accordingly.

Our report includes the program description and background information, scope, methodology, and procedures, objectives, conclusions, observations, recommendations, and management responses.

We appreciate the professional courtesy extended by your staff during this project. We are available to discuss appropriate corrective actions to help mitigate additional risks that may exist within this program or other departmental activities.

- c: Adam Sandoval, Deputy Director, LARA
- Kristen Staley, MIDC Executive Director, LARA
- Marla McCowan, MIDC Director of Training, Outreach and Support, LARA
- Rebecca Mack, MIDC Grants Director, LARA
- Sherri Washabaugh, Manager, OIAS

Table of Contents

Department of Licensing and Regulatory Affairs
Michigan Indigent Defense Commission
Consulting Report

Contents

| | |
|--|---|
| Program Description and Background Information | 1 |
| Scope, Methodology, and Procedures | 1 |
| Engagement Objective #1 | 2 |
| Observation #1: Manage Nonprofit Public Defender Offices as Subgrantees | 2 |
| Observation #2: Enhance Guidance to Local Systems for Monitoring Subgrantees | 3 |
| Engagement Objective #2 | 5 |
| Observation #3: Ensure Expenses Are Legitimate and Allowable | 5 |
| Appendix A – Classification of Conclusions and Observations | 7 |

Program Description and Background Information

The Michigan Indigent Defense Commission Act, PA 93 of 2013, established the MIDC to improve legal representation for indigent criminal defendants. The governor appoints 18 members to the commission, which selects an executive director to supervise 14 full-time staff, including six regional managers working statewide. MIDC develops and implements minimum standards for local systems providing indigent defense services and collects data, supports compliance, administers grants, and encourages best practices to accomplish its mission.

Local systems develop and submit plans each fiscal year to comply with standards established by MIDC to provide indigent defense. MIDC coordinates with each local system to review its compliance plans and approve a reasonable grant amount to be issued. Local systems are required to comply with the approved plan and cost analysis, which identifies budget categories, after receipt of the grant to provide effective counsel in compliance with standards. The commission approved and administered grants totaling \$117 million in fiscal year 2020.

Local systems may choose to provide indigent defense services by contracting with nonprofit entities, thereby creating nonprofit public defender offices (NPDO). Because these third parties pose increased risk of noncompliance with the terms of the grant agreement, it is necessary for MIDC and local systems to implement a robust system of control and monitoring activities. 7 of 130 (5%) local systems utilized NPDOs in FY20 and received a combined \$31 million out of \$117 million (26%) of grant funding. We selected one of these local systems to review for this engagement.

Scope, Methodology, and Procedures

We conducted our consulting engagement in conformance with the *International Standards for the Professional Practice of Internal Auditing*. OIAS' mission is to enhance and protect government operations through risk-based, objective assurance, advice, and insight.

We conducted our review for the period of October 1, 2019 through September 30, 2020, which is the period of the FY20 grant agreements. Our engagement included obtaining and reviewing appropriate records and documents, and other auditing procedures as we considered necessary to satisfy our objectives. Based on the scope and the work needed to complete the engagement, OIAS completed the following procedures summarized below in the body of this report.

Engagement Objective #1

To assist MIDC with improving its guidance to local systems for managing financial oversight of subgrantees, including nonprofit public defender offices, in compliance with PA 0214 of 2018 and other applicable policies and procedures, laws, regulations, and guidelines.

Conclusion:

Improvement Needed

Factors Impacting Conclusion:

- The grant agreement template provides stringent requirements for subgrantees, but NPDOs are excluded from the definition of subgrantees.
- MIDC now requires local systems that utilize NPDOs to submit those NPDOs' budgets/cost analyses with the local systems' compliance plans.
- MIDC did not define nonprofit public defender offices as subgrantees and require local systems to manage them accordingly.
- There are opportunities for MIDC to enhance guidance to local systems for monitoring NPDOs.

To achieve this objective, OIAS:

- Interviewed MIDC and local system staff to obtain an understanding of grant oversight.
- Reviewed compliance plans, budgets, and supporting documentation when available.
- Utilized the Association of Government Accountants (AGA) Recipient Checklist for Determining if the Entity Receiving Funds Has a Contractor or Subrecipient Relationship, which is based on Code of Federal Regulations (CFR) Title 2 - Grants and Agreements Subtitle A - Office of Management and Budget Guidance for Grants and Agreements Chapter II – Office of Management and Budget Guidance Part 200 – Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards (Uniform Guidance), issued by the U.S. Office of Management and Budget (OMB).
- Reviewed requirements of the State of Michigan's Financial Management Guide (FMG), Part II, Chapter 24, Section 200, Subrecipient/Contractor Determination.
- Reviewed the Statewide Grants Framework (Framework) developed by OIAS and based on Office of Management and Budget Uniform Administrative Requirements, Cost Principles and Audit Requirements for Federal Awards, 2CFR Part 200 within the Electronic Code of Federal Regulations.

Observation #1: Manage Nonprofit Public Defender Offices as Subgrantees

Risk Classification: Moderate

MIDC and local systems managed NPDOs as contractors instead of subgrantees, which reduces the level of oversight local systems are required to exercise over their public defender offices.

As part of our review, we created a spreadsheet using the AGA's checklist and answered the questions on the form in consultation with MIDC. We determined that NPDOs should be classified as subrecipients (subgrantees). The FMG requires State agencies to adhere to Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards when determining if a payee is a contractor or subrecipient. Although the Uniform Guidance is specific to federal grants and not required for grants issued by State agencies, this guidance provides a comprehensive framework for identifying grantee responsibilities and monitoring requirements.

Because NPDOs were not categorized as subgrantees, the parts of the grant agreement that dictate how subgrantees should be managed did not apply, including:

- Requirement that local systems include all terms and conditions of the grant agreement in any agreements with subgrantees. Without this requirement, contracts between local systems and subgrantees will not hold subgrantees to MIDC's terms and conditions, and subgrantees will not know what requirements they must comply with.
- Stipulation that local systems remain responsible for meeting the MIDC standards and adherence to the compliance plan. Without this stipulation, local systems may not sufficiently oversee their subgrantees under the belief that the risk of noncompliance with the grant agreement can be transferred to the subgrantees.
- MIDC's right to inspect and audit subgrantees. Without this right, MIDC cannot verify subgrantees are complying with the terms and conditions of the grant agreement.

The FY20 grant agreement between MIDC and local systems describes a subgrantee as "a governmental agency or other legal entity to which an MIDC subgrant is awarded by the Grantee." However, it specifically excludes "attorneys representing indigent defendants, including both public defenders and attorneys contracted to represent indigent defendants, public defender office employees, judges, magistrates, court personnel, and professional service contract vendors." According to our discussions with MIDC, this exclusion applies to NPDOs.

Recommendation:

We recommend that MIDC update its grant agreement template to include nonprofit public defender offices under its definition of subgrantees.

Management Response:

The Michigan Indigent Defense Commission (MIDC) agrees with the recommendation of the Office of Internal Audit Services and will change the language in the grant agreement template to reflect nonprofit public defender offices under its definition of subgrantees in the subsequent grant year.

Observation #2: Enhance Guidance to Local Systems for Monitoring Subgrantees

Risk Classification: Moderate

MIDC should enhance existing guidance to specify the monitoring activities that local systems are required to perform to ensure subgrantees spend funds appropriately and comply with the terms and conditions of the grant agreement.

Per the Framework, grantors must consider the risk of grant recipients being unaware of expectations, deliverables, and requirements related to the granting of funds. Additionally, grantors should establish guidelines and operating procedures for their grants.

During our review, we noted the following:

- The local system was unaware of its NPDO's policies and procedures over fraud, accounts payable, or conflict-of-interest. Without this knowledge, the local system cannot assess if the policies and procedures are appropriate for safeguarding MIDC dollars.
- The local system stated it monitored its NPDO by reviewing the NPDO's monthly invoices and program reports. These documents consisted of that month's case assignments and closings, as well as total expenses, which were broken out into salaries, benefits, and "other." This information does not provide sufficient detail for the local system to determine that the NPDO is adhering to required terms and conditions.
- We did not receive evidence of the local system's monitoring of its NPDO. As a result, we could not validate that the monitoring is taking place as intended.
- The local system did not require its NPDO to provide information related to potentially ineligible activities. The contract between the local system and its NPDO tasked the NPDO with addressing the civil and social needs that arose from clients' criminal cases; however, these services were not eligible to be paid for with the MIDC grant and had to be paid for with outside funding.
- The local system did not review its NPDO's proposed budget for compliance with the grant agreement. MIDC's review disclosed potentially ineligible expenses that the local system had not identified.

MIDC had not yet developed guidance for local systems to monitor subgrantees.

Recommendation:

We recommend that MIDC enhance existing guidance to specify the monitoring activities local systems are required to perform to ensure subgrantees comply with the terms and conditions of the grant agreement.

Management Response:

The MIDC agrees with the recommendation of the Office of Internal Audit Services and will provide enhanced and specific guidance to grantees that choose the nonprofit public defender model regarding the monitoring required by the local government. Our new grant management system is already designed to receive reporting from grant recipients and sub recipients and with training to local stakeholders can be implemented in the next grant year.

Engagement Objective #2

To review the allowability of expenses submitted for the MIDC grant program for the selected local system.

Conclusion:

Well-Controlled with Opportunities for Improvement

Factors Impacting Conclusion:

- The local system's FY20 Q3 financial status report reconciled to its general ledger.
- Some expenditures did not conform to the terms of the compliance plan.
- Local systems did not always submit documentation to support expenses or sufficiently monitor their vendors and subgrantees.

To achieve this objective, OIAS:

- Examined the local system's methodology for estimating personnel costs.
- Reconciled the local system's FY20 Q3 financial status report against its general ledger.
- Reviewed and tested documentation supporting expenses reported by the local system.

Observation #3: Ensure Expenses Are Legitimate and Allowable

Risk Classification: Low

Opportunities exist to ensure that MIDC funding is consistently used only for eligible expenses and these expenses are supported by appropriate documentation.

PA 0214 of 2018 requires MIDC to ensure "proper financial protocols in administering and overseeing funds utilized by indigent criminal defense systems." To this end, MIDC requires each local system to submit quarterly financial status reports (FSR). The FSR must be supported with documentation for the expenses, such as receipts, invoices, vouchers, and timesheets or a time study.

During our review, we noted that the local system had not provided supporting documentation to MIDC for the period October 1, 2019 through September 30, 2020. We obtained select invoices related to the Experts and Investigators cost analysis category and determined that 20 out of 77 (26%) payments totaling \$10,847 exceeded the expert and investigator hourly rates listed in the compliance plan; however, the MIDC Grant Manual does allow for higher expert and investigator rates when they are specifically authorized by a system on a case-by-case basis. We also noted 15 out of 77 (19%) payments included disallowed costs totaling \$2,654; some of these payments were disallowed by the funding unit's policies and procedures, not by MIDC. Additionally, we identified potential irregularities in four paid invoices.

In addition to testing the local system's invoices, we examined its methodology for estimating the number of jail deputies necessary to transport inmates to their initial visit meetings with their attorneys and the amount of time those transportations take. The local system was charging the grant for the personnel expenses of the jail deputies' wages. Although the local system provided a spreadsheet from the Sheriff's Office listing the number of deputies required for each jail, the spreadsheet does not explain how the Sheriff's Office determined these numbers. The local system did not conduct a time study or evaluate the increase in initial attorney visits since the MIDC standard requiring initial visits was implemented.

We also noted that the local system claimed \$326,722 for indirect costs. The compliance plan does allow the local system to claim 10% of total personnel expenses as indirect costs; however, FY20 total personnel costs amounted to \$2,417,601, 10% of which is \$241,760. Therefore, the local system claimed \$84,962 more in indirect costs than it was entitled to.

MIDC has not consistently enforced the requirement that local systems provide documentation to support expenses. Additionally, local systems are not sufficiently monitoring their vendors and subgrantees.

Recommendation:

We recommend MIDC consistently enforce that local systems provide documentation to support expenses and ensure local systems sufficiently monitor vendors and subgrantees.

Management Response:

The MIDC agrees with the recommendation of the Office of Internal Audit Services and will work with grantees to ensure proper documentation is submitted to support grant expenses. This task has been made difficult in the past year to manage with substantial increases in grant awards and complexity of grants, a very manual grant management system and a long term vacancy in the Grant's Department due to a state mandated hiring freeze. The MIDC will also pursue reclaiming the excess indirect costs from the local government claimed in the FY20 grant year.

The MIDC has launched a new grant management system, EGrAMS, that will shift the focus to online reporting of grant activities with documentation uploads that will aid in the process of a more efficient financial compliance review. EGrAMS went live for FY22 grant applications and post contract grant administration will be implemented with the first reporting due in January 2022.

The MIDC would like to thank the Office of Internal Audit Services for its diligence in reviewing our grant management system and their recommendations for improvements. The coordination and feedback between the agencies has been valuable and will lead to positive change for our grant management, data collection, decision making and reporting.

Appendix A – Classification of Conclusions and Observations

Classification of Audit Objective Conclusions

| Conclusion | Description of Factors |
|---|---|
| Well-Controlled | The processes are appropriately designed and are operating effectively to manage risks. Control issues may exist but are low risk. |
| Well-Controlled with Opportunities for Improvement | The processes have design or operating effectiveness deficiencies but do not compromise achievement of important control objectives. Control issues exist but are low or medium risk. |
| Improvement Needed | The processes are not appropriately designed and/or are not operating effectively to manage risks. Control issues exist but are low or medium risk. Weaknesses are present that compromise achievement of one or more control objectives but do not prevent the process from achieving its overall purpose. |
| Major Improvement Needed | The processes are not appropriately designed and/or are not operating effectively to manage risks. Control issues exist and are medium or high risk. Weaknesses are present that could potentially compromise achievement of its overall purpose. |

Risk Classification of Audit Observations

| Rating | Description of Factors |
|-----------------|--|
| Low | Represents a process improvement opportunity. Observation poses relatively minor exposure to the program under review. |
| Moderate | Requires near-term department attention. Observation has moderate impact to the program. Compensating controls may exist but are not operating as designed. |
| High | Requires immediate department attention and remediation. Observation has broad (state or department wide) impact and possible or existing material exposure. |