

Audit Report

**Department of Public Safety and Correctional Services
Maryland Correctional Enterprises**

October 2019



OFFICE OF LEGISLATIVE AUDITS
DEPARTMENT OF LEGISLATIVE SERVICES
MARYLAND GENERAL ASSEMBLY

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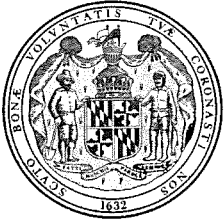
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DEPARTMENT OF LEGISLATIVE SERVICES
OFFICE OF LEGISLATIVE AUDITS
MARYLAND GENERAL ASSEMBLY

Victoria L. Gruber
Executive Director

Gregory A. Hook, CPA
Legislative Auditor

October 31, 2019

Senator Craig J. Zucker, Senate Chair, Joint Audit and Evaluation Committee
Delegate Shelly L. Hettleman, House Chair, Joint Audit and Evaluation Committee
Members of Joint Audit and Evaluation Committee
Annapolis, Maryland

Ladies and Gentlemen:

We have conducted a fiscal compliance audit of the Maryland Correctional Enterprises (MCE) for the period beginning February 20, 2015 and ending March 31, 2019. MCE, which is a unit within the Department of Public Safety and Correctional Services (DPSCS), provides work and job training for inmates of the Maryland correctional system.

Our audit disclosed that MCE did not always investigate and resolve variances between its materials and supplies inventory records and the amounts on hand; rather, MCE simply adjusted the inventory records without any supervisory review and approval.

Our audit also included a review to determine the status of the three findings contained in our preceding audit report. We determined that MCE satisfactorily addressed two of these three findings. The remaining finding is repeated in this report.

DPSCS' response to this audit, on behalf of MCE, is included as an appendix to this report. We reviewed the response to our finding and related recommendations, and have concluded that the corrective actions identified are sufficient to address all audit issues.

We wish to acknowledge the cooperation extended to us during the audit by MCE. We also wish to acknowledge DPSCS' and MCE's willingness to

address the audit issues and implement appropriate corrective actions.

Respectfully submitted,

A handwritten signature in black ink that reads "Gregory A. Hook". The signature is written in a cursive style with a large, prominent initial "G".

Gregory A. Hook, CPA
Legislative Auditor

Background Information

Agency Responsibilities

The Maryland Correctional Enterprises (MCE) is organized under the State of Maryland's Department of Public Safety and Correctional Services (DPSCS). MCE operates under the provisions of the Correctional Services Article of the Annotated Code of Maryland. The Correctional Services Article provides, in part, that MCE develop programs that provide work experience or rehabilitation for eligible inmates. The Correctional Services Article also provides that MCE be financially self-supporting. The goods produced (for example, furniture, metal products, mattresses, and printing) and services offered (for example, inmate laundry) by MCE are available to State and federal agencies, political subdivisions, and any charitable, civic, educational, fraternal, or religious agency, association, or institution (for their own use and not for resale to others), or as otherwise indicated in the law.

According to MCE's audited financial statements, MCE's fiscal year 2018 operating revenue and operating expenses were approximately \$55 million and \$51.2 million, respectively, and its net operating income for fiscal year 2018 totaled \$3.8 million. As of June 30, 2018, MCE's net position totaled \$30.2 million.

Financial Statement Audits

For fiscal years 2015, 2016, 2017, and 2018, MCE engaged an independent accounting firm to perform the audit of MCE's financial statements. In the related audit reports, the firm stated that MCE's financial statements presented fairly, in all material respects, the respective financial position of MCE and the respective changes in its financial position and its cash flows for the years then ended, in accordance with accounting principles generally accepted in the United States of America.

Number of Inmates Employed by MCE Has Declined

MCE's *Fiscal Year 2018 Annual Report*, submitted to the Governor, disclosed that the number of inmates employed in its enterprise programs had decreased from 2,042 in fiscal year 2017 to 1,719 in fiscal year 2018. The *Report* attributed this decrease to staff vacancies and the lack of qualified MCE civilian staff to supervise the inmates. Specifically, MCE needs to maintain a safe staff-to-inmate

ratio and has had difficulty filling the supervisor positions with staff skilled in trades such as metal, upholstery, and woodworking.

During the 2019 legislative session, DPSCS (on behalf of MCE) advised the General Assembly’s budget committees that the decline in the Statewide inmate population had resulted in a reduced demand for MCE goods and services by the inmate population (such as clothing, furniture, bedding and linen, and laundry services). Consequently, DPSCS advised the budget committees that MCE is projecting to employ 1,700 inmates during fiscal years 2019 and 2020, which is below MCE’s Managing for Results goal of 2,100 inmate employees.

Status of Findings From Preceding Audit Report

Our audit included a review to determine the status of the three findings contained in our preceding audit report dated July 24, 2015. As disclosed in the table below, we determined that MCE satisfactorily addressed two of these findings. The remaining finding is repeated in this report.

Status of Preceding Findings		
Preceding Finding	Finding Description	Implementation Status
Finding 1	Proper controls had not been established over mail receipts.	Not Repeated
Finding 2	MCE lacked adequate controls over non-cash credit adjustments.	Not Repeated
Finding 3	MCE had no documentation of supervisory review and approval of adjustments to inventory records.	Repeated (Current Finding 1)

Findings and Recommendations

Materials and Supplies

Finding 1

MCE did not always investigate and resolve variances between its materials and supplies inventory records and the amounts on hand.

Analysis

MCE did not always investigate and resolve variances between its materials and supplies inventory records and the amounts on hand. Rather, MCE adjusted the inventory records to reflect the amounts on hand without any investigation or supervisory review and approval. The materials and supplies inventory balance reported to DGS as of June 30, 2018 totaled approximately \$10.5 million.

MCE's fiscal year 2018 reconciliation of its finished goods inventory records with the amounts on hand identified 89 variances in excess of \$5,000, totaling approximately \$1.4 million. Our review disclosed that MCE did not investigate 57 of these variances totaling \$1.1 million; rather, MCE simply adjusted the inventory records without any supervisory review and approval. MCE management advised us that it had not investigated these variances due to staff shortages.

The Department of General Services' (DGS) *Inventory Control Manual* requires that all variances between inventory records and the amounts on hand be investigated and that the adjustments to the related inventory records be approved by someone in authority not below the level of Chief Administrative Officer. The lack of documented supervisory review of the investigations and the related adjustments was commented upon in our preceding audit report.

Recommendation 1

We recommend that MCE ensure that

- a. inventory variances are investigated and resolved, and**
- b. the investigations and related inventory record adjustments are reviewed and approved by appropriate supervisory personnel (repeat).**

Audit Scope, Objectives, and Methodology

We have conducted a fiscal compliance audit of the Maryland Correctional Enterprises (MCE), a unit within the Department of Public Safety and Correctional Services (DPSCS), for the period beginning February 20, 2015 and ending March 31, 2019. The audit was conducted 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.

As prescribed by the State Government Article, Section 2-1221 of the Annotated Code of Maryland, the objectives of this audit were to examine MCE's financial transactions, records, and internal control, and to evaluate its compliance with applicable State laws, rules, and regulations.

In planning and conducting our audit, we focused on the major financial-related areas of operations based on assessments of significance and risk. The areas addressed by the audit included purchases and disbursements, cash receipts, accounts receivable, materials and supplies, and equipment. We also determined the status of the findings contained in our preceding audit report.

Our audit did not include certain support services provided to MCE by the DPSCS – Office of the Secretary. These support services (such as processing of human resource transactions and procurement of certain information technology related contracts) are included within the scope of our audit of the DPSCS – Office of the Secretary.

To accomplish our audit objectives, our audit procedures included inquiries of appropriate personnel, inspections of documents and records, observations of MCE's operations, and tests of transactions. Generally, transactions were selected for testing based on auditor judgement, which primarily considers risk. Unless otherwise specifically indicated, neither statistical nor non-statistical audit sampling was used to select the transactions tested. Therefore, the results of the tests cannot be used to project those results to the entire population from which the test items were selected.

We also performed various data extracts of pertinent information from the State's Financial Management Information System (such as revenue and expenditure data). The extracts are performed as part of ongoing internal processes established by the Office of Legislative Audits and were subject to various tests to

determine data reliability. We determined that the data extracted from this source were sufficiently reliable for the purposes the data were used during this audit. We also extracted data from MCE's financial and manufacturing management system (MAPICS) for the purpose of selecting test items and assessing user access. We performed various tests of the relevant data and determined that the data were sufficiently reliable for the purposes the data were used during the audit. Finally, we performed other auditing procedures that we considered necessary to achieve our objectives. The reliability of data used in this report for background or informational purposes was not assessed.

MCE's management is responsible for establishing and maintaining effective internal control. Internal control is a process designed to provide reasonable assurance that objectives pertaining to the reliability of financial records; effectiveness and efficiency of operations, including safeguarding of assets; and compliance with applicable laws, rules, and regulations 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.

Our reports are designed to assist the Maryland General Assembly in exercising its legislative oversight function and to provide constructive recommendations for improving State operations. As a result, our reports generally do not address activities we reviewed that are functioning properly.

This report includes a finding relating to a condition that we consider to be a significant deficiency in the design or operation of internal control that could adversely affect MCE's ability to maintain reliable financial records, operate effectively and efficiently, and/or comply with applicable laws, rules, and regulations. This finding is also regarded as a significant instance of noncompliance with applicable laws, rules, or regulations. Other less significant findings were communicated to MCE that did not warrant inclusion in this report.

The response from DPSCS, on behalf of MCE, to our finding and recommendation is included as an appendix to this report. As prescribed in the State Government Article, Section 2-1224 of the Annotated Code of Maryland, we will advise DPSCS regarding the results of our review of its response.

APPENDIX



Department of Public Safety and Correctional Services

Office of the Secretary

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CAROLYN J. SCRUGGS
ASSISTANT SECRETARY

GARY W. McLHINNEY
ASSISTANT SECRETARY

October 28, 2019

Gregory A. Hook, CPA
Office of Legislative Audits
301 West Preston Street, Room 1202
Baltimore, Maryland 21201

Dear Mr. Hook,

We have reviewed the October 11, 2019 Draft Legislative Audit Report for the Department of Public Safety and Correctional Services' (DPSCS) Maryland Correctional Enterprises (MCE), and we are pleased that two of the three findings from the last audit have been satisfactorily addressed. The Department appreciates the constructive recommendations that were provided as the result of this audit.

Attached is MCE Chief Executive Officer Stephen M. Shiloh's response to the Draft Audit Report. Mr. Shiloh will continue to implement corrective action to resolve the audit finding, and the Office of the Inspector General will conduct periodic follow up audits to verify the status of compliance.

If you have any questions regarding this response, please contact me.

Sincerely,

A handwritten signature in black ink, appearing to read "Robert L. Green".

Robert L. Green
Secretary

Attachments

Cc: Walter Pete Landon, Deputy Chief of Staff



Department of Public Safety and Correctional Services

Maryland Correctional Enterprises

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COMMISSIONER

MARYLAND CORRECTIONAL
ENTERPRISES

STEPHEN M. SHILOH, CCE
CHIEF EXECUTIVE OFFICER

October 28, 2019

The Honorable Robert L. Green, Secretary
Department of Public Safety & Correctional Services
300 East Joppa Road, Suite 1000
Towson, Maryland 21286-3020

Via

Mr. J. Michael Zeigler, Deputy Secretary Operations
Department of Public Safety & Correctional Services
300 East Joppa Road, Suite 1000
Towson, Maryland 21286-3020

Attached is the Maryland Correctional Enterprises (MCE) response to the Draft Legislative Audit report dated October 11, 2019, covering the examination of MCE's financial transactions, records and internal controls, and the evaluation of compliance with applicable State laws, rules, and regulations for the period beginning February 20, 2015 and ending March 31, 2019. MCE will implement corrective action to resolve the finding mentioned in the report.

MCE would like to acknowledge the cooperation and professionalism demonstrated by the Office of Legislative Audits during the course of this audit.

Sincerely,
Stephen M. Shiloh, CCE
Chief Executive Officer

CC: Chris McCully, Deputy Secretary for Administration
Joseph M. Perry, Inspector General
Wayne Hill, Commissioner
Mark K. Rowley, Chief Administrative Officer
Verona M. Williams, Chief Financial Officer

**Department of Public Safety and Correctional Services
Maryland Correctional Enterprises**

Agency Response Form

Materials and Supplies

Finding 1

MCE did not always investigate and resolve variances between its materials and supplies inventory records and the amounts on hand.

We recommend that MCE ensure that

- a. inventory variances are investigated and resolved, and**
- b. the investigations and related inventory record adjustments are reviewed and approved by appropriate supervisory personnel (repeat).**

Agency Response			
Analysis			
Please provide additional comments as deemed necessary.			
Recommendation 1a	Agree	Estimated Completion Date:	8/1/2020
Please provide details of corrective action or explain disagreement.	MCE will ensure that inventory variances are investigated, and to the extent possible, will resolve them.		
Recommendation 1b	Agree	Estimated Completion Date:	8/1/2020
Please provide details of corrective action or explain disagreement.	MCE will ensure the investigations and the related inventory record adjustments are reviewed and approved by appropriate supervisory personnel.		

AUDIT TEAM

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