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April 30, 2002

To: Supervisor Zev Yaroslavsky, Chairman
Supervisor Gloria Molina
Supervisor Yvonne Brathwaite Burke
Supervisor Don Knabe
Supervisor Michael D. Antonovich

From: J. Tyler McCauley
Auditor-Controller

Subject: **FISCAL REVIEW OF LIDDELL'S GROUP HOME - A GROUP HOME FOSTER CARE CONTRACTOR**

Attached is our audit report on Liddell's Group Home (Liddell's) fiscal operations for the period January 1, 2000 through June 30, 2001. Liddell's is currently licensed to operate one group home with a resident capacity of ten children. Liddell's is located in the First Supervisorial District. During the 18-month period reviewed, Liddell's received approximately $626,000 in group home funds from the Department of Children's Services DCFS).

Summary of Findings

Our audit disclosed a number of deficiencies in Liddell's system of internal control over the disbursement of group home funds, including inadequate and incomplete accounting records. As a result, we have questioned a total of $91,395 in expenditures made by Liddell's with group home funds during the 18-month audit period. In addition, we noted several instances where remittances from the County totaling $6,858, could not be traced into the Agency's bank records.

The questioned costs consist primarily of expenditures for which Liddell's either provided no supporting documentation, or the supporting documentation provided was not adequate. The questioned costs also include expenditures of group home funds for purposes that are considered unallowable under the applicable guidelines.

DCFS should ensure that the Agency's management takes appropriate, timely corrective actions to address the recommendations in this report and monitor to ensure full implementation of corrective actions.

Review of Report

We discussed our report with Liddell's management on March 26, 2002. They have agreed to provide DCFS with a written response and corrective action plan within 30 days. In addition, DCFS has agreed to provide my office with a written response within 60 days detailing the resolution of all findings contained in the report.

We would like to thank Liddell's management and staff for their cooperation during our review.

JTM:DR:MM

Attachment

c: David E. Janssen, Chief Administrative Officer
Department of Children and Family Services
Anita Bock, Director
Ed Sosa, Chief, Out of Home Care Programs
Genevra Gilden, Chief, Quality Assurance Division
Commission for Children and Family Services
Liddell's Group Home
Jerry Liddell, Executive Director
Board of Directors
California Department of Social Services
Sharon Ferrante, Chief, Foster Care Audits Bureau
Evelyn Hemenover, Chief, Foster Care Rates Bureau
Public Information Office
Audit Committee

LIDDELL'S GROUP HOME, INC.
FISCAL AUDIT OF GROUP HOME FOSTER CARE CONTRACT

SCHEDULE OF FINDINGS

BACKGROUND

The Department of Children and Family Services (DCFS) contracts with Liddell's Group Home Inc. (Liddell's) to provide the basic needs and services for foster care children placed in the Agency's care. Liddell's is located in the First Supervisorial District and is licensed to operate one group home with a capacity of ten children.

Under the provisions of its contract with Liddell's, the County pays Liddell's a monthly rate for each child based on rate classification levels determined by the California Department of Social Services (CDSS). Liddell's received a monthly rate of between $3,521 and $3,912 per child during the period of our audit, January 1, 2000 through June 30, 2001, for a total of $625,594 in foster care funds.

SCOPE

The purpose of our audit was to determine whether Liddell's complied with its County contract and appropriately accounted for and spent foster care funds on necessary, allowable, and reasonable expenditures in providing contract services to children placed in the Agency's care. We tested a sample of Liddell's expenditures, both payroll and non-payroll expenditures to ensure that the Agency maintained appropriate documentation to support the expenses. We also evaluated the adequacy of the Agency's accounting records, internal controls, and compliance with applicable federal and CDSS fiscal guidelines governing the disbursement of group home foster care funds.

Liddell's was unable to provide us with supporting documentation for almost one-half of the non-payroll transactions we selected. We selected 63 non-payroll transactions for review. The 63 transactions represent approximately 24% of the Agency's total non-payroll disbursements. Liddell's was unable to provide us with adequate support for 30 (48%) of the 63 transactions.

Applicable Regulations and Guidelines

Liddell's is required to operate its group homes in accordance with certain federal, State and County regulations and guidelines. We referred to the following applicable regulations and guidelines during our audit:

- Group Home Foster Care Contract (Contract), including Exhibit D, DCFS Contract Accounting and Operating Handbook (DCFS Handbook).
- Federal Office of Management and Budget Circular A-122, Cost Principles for Non-Profit Organizations (Circular).
- California Department of Social Services Manual of Policies and Procedures (CDSS MPP).
- California Code of Regulations, Title 22 (Title 22).

QUESTIONED COSTS/REVENUES

Our review disclosed a number of deficiencies in Liddell's system of internal control over group home funds and expenditure practices, including incomplete accounting records and a lack of supporting documentation. These deficiencies resulted in questioned costs totaling $91,395 during the 18-month audit period. In addition, we noted several instances where County remittances totaling $6,858 could not be traced into the Agency's bank records. Details of the questioned costs and unaccounted revenues are discussed in three sections below: Unsupported/ Inadequately Supported Costs, Unallowable Costs, and Unaccounted Revenues.

Unsupported/Inadequately Supported Costs

We identified group home expenditures totaling $62,725 that Liddell's was either unable to provide supporting documentation for, or the support provided was inadequate.

- $18,463 in payments for items such as food, household items, utilities, telephone, cellular phone, equipment & equipment lease, office rent, maintenance, employee benefits, insurance, supplies, clothing, audit fees, postage, and reimbursements to Executive Director and Administrator (who are husband and wife), and for various cash withdrawals from the Agency's checking account. Of the total costs questioned, the agency provided no support for $7,308 (40%) in disbursements. The remaining $11,155 (60%) was not adequately supported by invoices or receipts.
- $20,592 in disbursements were unclassified by the Agency in their accounting records. These expenditures had been charged to a Suspense account in the Agency's general ledger and appear to be primarily for personal credit card payments and loans. The agency was unable to provide us with supporting documentation for these disbursements.
- $10,715 in automobile expenses including lease payments, gasoline, repairs and maintenance bills for two vehicles owned by the Executive Director and the

Administrator. The Agency did not maintain a copy of the lease agreement, nor were records kept to document the Agency's business use of the vehicle as required by the DCFS Handbook, Section A (ACCOUNTING AND FINANCIAL REPORTING) Subsection 3.2. While some of these costs were undoubtedly incurred for the benefit of group home, we were unable to determine which portions were allocable to the group home because the Agency did not maintain the required documentation. Accordingly, we are questioning the entire amount.

- $7,468 in advance payroll payments made to 11 Agency employees between January 2000 and June 2001 which had not been recovered as of June 30, 2001.

- $3,787 in repayments, to the Executive Director and Administrator, for loans that we could not validate. The Agency indicated that Executive Director and the Administrator made payments on behalf of the Agency totaling $22,770 during the period being audited. During this same period, the Agency issued reimbursements totaling $6,863, reportedly as partial repayment of these loans.

  We were able to confirm only $3,076 of the $22,770 in loans the Agency reported it received from the Executive Director and Administrator. The Agency did not maintain loan agreements with either the Executive Director or the Administrator. Further, Liddell's management could not document that the loan proceeds were deposited into the group home's bank accounts, due to the absence of duplicate bank deposit tickets (this is discussed further in the "Other Issues" section of this report), nor could the Agency produce the cancelled personal checks of the Executive Director and Administrator to substantiate the loans. Because the Agency was unable to document the full amount of the loans, we are questioning $3,787, the difference between the amounts repaid ($6,863) and the loan amount we were able to confirm ($3,076).

- $1,700 in salary payments to the Executive Director was not supported by timecards or other documentation.

Unallowable Expenditures

We identified $28,670 in unallowable group home expenditures. Below are the details of these questioned expenditures.

Excess Salary Costs

Based on the CDSS MPP Section 11-402, the salary of the Agency's Administrator for the 18 months is capped at 86.2% of the Executive Director's salary of $66,215 for the period, or $57,077. The Administrator was actually paid $66,215 for the 18-month audit period. Accordingly, we are questioning the $9,138 difference between the amount paid and the salary cap amount.

Interest and Penalties

Liddell's used group home funds for $8,823 in penalties and interest paid to the Internal Revenue Services for delinquent payroll taxes as of December 31, 2000. The Agency also used group home funds totaling $2,742 to pay penalties and fees associated with its bank account (e.g., overdraft, returned checks, non-sufficient funds, etc.) and late rental payment for its administrative office. According to Circular A-122, fines, penalties and late charges resulting from violations of federal, state, and local laws and regulations are not allowable.

Excess Shelter Costs

CDSS MPP Section 11-402.828 states that group home shelter costs shall not exceed 12% of the fair market value shown on the last property tax bill, or a recent property appraisal. Shelter costs include, but are not limited to, mortgages for owned property, lease or rental costs, capital improvements, taxes, building insurance and appraisals for owned, leased or rented property.

Liddell's shelter costs consist of monthly rent for one group home, which is owned by the Agency's Executive Director and Administrator. During the period being audited, Liddell's charged $39,135 in shelter costs. We determined that based on a recent independent appraisal, the shelter costs charged represented approximately 14.5% of the home's fair market value, or $6,735 in excess of the amount allowed per State regulations.

Agency Administrator Reimbursement

The Agency's Administrator was reimbursed $1,232 for checks written to two Agency employees from her personal account. According to management, the Agency was experiencing cash flow difficulties in November 2000 and was unable to issue payroll checks to the two employees with Agency funds. The Administrator paid the employees from her personal account. However, our review of payroll records and bank statements indicated that the employees' salaries were paid by Agency checks for this period.

Unaccounted Revenues

We were unable to verify that 13 regular and supplemental remittances from the County, totaling $6,858, were used for allowable group home expenses. Of the 13 remittances, we determined that seven totaling $1,249 were cashed at a grocery store. While we were able to verify that the six remaining remittances totaling $5,609 were negotiated, we could not verify that the payments were deposited into the Agency's bank account. Since we were unable to verify that these remittances were deposited into Liddell's bank account, we could not determine if the funds were used for allowable group home expenses.

Recommendations

1. **DCFS management resolve the $98,253 in questioned costs and unaccounted revenues and, if appropriate, collect any disallowed amounts.**

To appropriately account for Group Home funds and administer the Group Home program in compliance with the terms of its agreement with the County, the Agency must implement the following recommendations.

Liddell's management:

2. **Maintain adequate supporting documentation for all group home expenditures, including original itemized invoices and receipts.**

3. **Ensure that group home funds are used only for necessary, allowable and reasonable expenditures to carry out the purpose and activities of the group home.**

4. **Maintain detailed vehicle mileage logs for all Agency vehicles.**

5. **Ensure that employee timecards are consistently prepared.**

6. **Ensure shelter and salary costs do not exceed the maximum allowed by State regulations.**

INTERNAL CONTROL WEAKNESSES

Our audit disclosed several internal control weaknesses and contract compliance issues in addition to those already mentioned. These deficiencies contributed to the questioned expenditures discussed above. DCFS must ensure that Liddell's management takes appropriate corrective actions to address each recommendation included in this report. DCFS should also monitor this contractor to ensure that the corrective action measures result in permanent changes to the Agency's operations.

Controls Over Disbursements and Revenues

- Liddell's routinely uses its petty cash fund to pay normal operating expenses of the Agency. During the audit period, it was a normal practice for Agency officers and employees to incur expenses on behalf of the Agency and later receive a reimbursement check. However, the reimbursement check amount often did not agree with the total of receipts and invoices provided to support the payment.

Agency management stated that, in some instances, Agency personnel purchased cashier's checks with their own funds to pay certain vendors that would not accept an Agency check. The employees were subsequently reimbursed by the Agency. However, we noted at least one instance where a cashier's check purchased was payable to Agency personnel, which calls this explanation into question.

- Documentation (invoices, receipts, etc.) to support 19 of 52 (37%) non-payroll expenditures for which documentation was provided was not marked "paid" or otherwise cancelled to prevent re-use. Similarly, supporting documentation for 27 of 52 (52%) expenditures was not cross-referenced to the corresponding disbursement (i.e., check number).

- Seven of 52 (13%) non-payroll expenditures were not properly classified in the Agency's accounting records. These expenditures should be recorded according to the nature of the transaction.

- In many instances, the Administrator prepared and signed checks made payable to herself. To ensure all disbursements are appropriate, Liddell's Board of Directors should designate an alternate check signer, preferably a Board member, to sign all checks issued to the Administrator.

- Checks were not used in sequential order and voided checks were not retained. Liddell's management should ensure checks are used in sequential order and voided checks are kept on-hand to assist in establishing accountability over the sequence of checks issued.

- The Agency did not maintain an accounts receivable ledger to account for payments due from DCFS. Without a ledger, there is increased risk that amounts payable to the Agency could remain outstanding and go undetected.

- The Agency did not regularly maintain duplicate bank deposit slips/receipts for deposit of all funds received from DCFS, making it difficult to reconcile remittances received from DCFS to amounts deposited per the Agency's bank statements.

Without proper internal controls in place, there is reduced assurance that group home funds will be properly accounted for, controlled, and spent on actual, reasonable and allowable expenses in providing the necessary care and services to children placed in the group home.

Recommendations

Liddell's management:

7. **To the extent possible, discontinue the practice of using petty cash to fund normal daily operations. When petty cash is used, ensure amounts reimbursed equal the receipts and invoices submitted with the request for reimbursement.**

8. **Ensure invoices and receipts are consistently marked "PAID" to prevent reuse, cross-referenced to corresponding check numbers and filed in a systematic fashion to permit easy retrieval.**

9. **Ensure expenditures are properly classified in the Agency's accounting records.**

10. **Ensure Agency's Board of Directors designate an alternate check signer, preferably a Board member, to sign all checks issued to the Administrator.**

11. **Ensure that checks are used in sequential order and voided checks are retained to assist in establishing accountability over the sequence of checks used.**

12. **Ensure that the Agency maintains an accounts receivable ledger.**

13. **Maintain duplicate bank deposit slips/receipts for deposit of all funds received from DCFS.**

Controls Over Bank Accounts

We observed that the Agency does not have a formal policy specifying the frequency of bank deposits. For example, we noted an instance where a check for $2,790 was received on April 27, 2000, but was not deposited until June 7, 2000, forty days later. There were other instances were deposits in excess of $500 were not made timely. According to Agency management, deposits are usually made weekly, or when large collections are accumulated. To ensure adequate security over group home funds, the Agency should make deposits daily, or when collection amounts reach $500, in accordance with the DCFS Handbook. In no case should deposits be less frequent than weekly.

We also noted that Liddell's staff does not sign and date their bank reconciliations. Therefore, we were unable to determine if bank reconciliations were completed timely and reviewed by management for appropriateness and accuracy. Section B (INTERNAL CONTROLS), Subsection 1.4, of the DCFS Handbook states that monthly bank reconciliations should be prepared within 30 days of the bank statement date and reviewed by management for appropriateness and accuracy. Both the preparer and the reviewer should sign and date the bank reconciliations. Also, during the audit period, significant NSF charges were incurred. Timely reconciliations should prevent this from occurring in the future.

Recommendations

Liddell's management ensure that:

14. Bank deposits are made daily, or when collection amounts reach $500.

15. Bank reconciliations are completed timely, and are signed and dated by the preparer and reviewer.

Payroll/Personnel Controls

Liddell's payroll and personnel procedures are not in compliance with the Circular, CDSS MPP, Title 22 and the DCFS Handbook. We tested 12 separate employees' timecards and found the following:

- Personnel files reviewed did not, in all cases, contain authorized salary amounts, or hourly rates of pay approved by management. CDSS MPP Section 11-402 requires that supporting documentation be maintained for all program expenditures including employee salary rates.

- Supervisors did not sign time cards indicating that they had been reviewed and approved and only three of twelve employees signed their time cards certifying the accuracy of time reported.

- The Agency did not maintain appropriate records of benefit balances earned (e.g., vacation hours earned) and used.

- Employee salary advances were not documented. Salary advances were recorded in the Agency's general ledger. However, the reasons for the advances and management's approval of the advances were not documented. Also, as noted in the "Unsupported/Inadequately Supported Costs" section, salary advances were not always recovered.

Proper payroll and personnel controls will help ensure that Agency payroll expenditures are authorized and accurate.

Recommendations

Liddell's management:

16. **Ensure Agency personnel files contain authorized salary amounts, or hourly rates of pay approved by management.**

17. **Ensure employees certify the time reported on their timecards by signing the timecards and require that all timecards be reviewed and approved in writing by management.**

18. **Maintain appropriate logs to calculate benefit balances.**

19. **Document the reasons for and management approval of salary advances.**

CONTRACT COMPLIANCE

Daily Attendance Logs

The Agency did not maintain a daily attendance log for residents as required in its contract with the County.

Recommendation

20. **Liddell's management ensure that all records required by the contract such as a daily attendance log are maintained.**

Insurance Coverage

Liddell's did not submit an insurance confirmation to substantiate insurance coverage in accordance with Contract Section 22 for general, auto, professional and worker's compensation liability.

Recommendation

21. **DCFS management take action to ensure Liddell's has insurance coverage required by Contract Section 22.**

OTHER ISSUES

In addition to the internal control and contract compliance issues previously discussed, our review also disclosed other concerns with group home loans, leases of household items, records of donated items and compliance with payroll tax laws.

Group Home Loans

As previously discussed in the "Questioned Costs" section of this report, we were unable to validate $19,694 of $22,770 in loans reportedly made to the Agency during the audit period by the Agency's Administrator. Liddell's does not have a written loan agreement and management was unable to document that the Agency received the loan proceeds, or deposited them into one of the Group Home's bank accounts. As part of our questioned costs, we have questioned loan repayments made during the audit period to the extent they exceed the portion of the loans that we were able to validate. Liddell's should not use group home funds to repay the unsupported liability unless Agency management can adequately document and prove to DCFS that the loan proceeds were deposited into the one of the Agency's bank accounts and were used for necessary, allowable and reasonable costs of the Group Home.

Recommendation

22. Liddell's management not use group home funds to repay $19,694 in loans unless Agency management can adequately document and prove to DCFS the receipt and deposit of the loan proceeds to the Agency's bank account.

Rental of Household Items

During the audit period, the Agency incurred approximately $5,000 in expenditures for the monthly rental of household entertainment equipment such as a large screen television, a Digital Video Disk (DVD) and Video Cassette Recorder (VCR) and other household equipment such as a washing machine and a dryer for the group home foster children. According to management, the Agency's policy has always been to rent household equipments for the group home. However, as these monthly rental payments will continue to be incurred, it might be more economical for the Agency to purchase these items instead of renting them.

Recommendation

23. Liddell's management evaluate the propriety of continuing to lease household items.

Records of Donated Items

Liddell's receives donations of video games, educational games, gift certificates and other items to be used by group home children. However, the Agency does not maintain records documenting the items donated and which children the items were given to. In order to adequately account for these donated items, the Agency should maintain records for all items donated along with the disposition of those items.

Recommendation

24. Liddell's management maintain records to account for the receipt and distribution of all donated items.

Compliance with Federal and State Payroll Tax Laws

Liddell's has not remitted payroll taxes and employee tax withholdings to the IRS and State Franchise Tax Board for calendar years 1997 and 1998. According to Liddell's Administrator, the Agency was experiencing cash flow problems due to unfilled beds and, therefore, was unable to meet its tax obligations. As of June 30, 2001, the Agency owed the IRS $16,175 and had negotiated a repayment agreement for this amount.

Although the Agency has taken steps to resolve its obligations to the federal and State taxing agencies, the required payment could result in the group home experiencing additional cash flow problems. Potentially, this could ultimately impact the Agency's ability to provide quality care and services to the children in the future. Also, of the $16,175 owed to the IRS, $8,664 is for penalties and interest. DCFS management should ensure that the Agency does not use group home funds to pay penalties and interest assessed on their debt to the IRS.

Recommendation

25. DCFS ensure that Liddell's does not use group home funds to pay for penalties and interest on their debt to the IRS and State Franchise Tax Board.