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DEPARTMENT OF AUDITOR-CONTROLLER

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October 14, 2003

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

FROM: J. Tyler McCauley
Auditor-Controller

SUBJECT: **REVIEW OF NEW CONCEPT GROUP HOME – A GROUP HOME FOSTER CARE CONTRACTOR**

Attached is our report on New Concept Group Home (New Concept or Agency) fiscal operations for the period January 1, 2002 through December 31, 2002. New Concept is one of two group homes licensed to operate under the corporate name of Humanistic Foundation, Incorporated. The other group home, Stockdale Boys Center, is located in Kern County. New Concept has a resident capacity of eight children and, during our review period, received $335,084 from Los Angeles County. The Los Angeles County facility is located in the Second Supervisorial District.

Scope

The purpose of our review was to ensure that New Concept has complied with the contract and appropriately accounted for and spent foster care funds on allowable and reasonable expenditures in providing services to children placed in the Agency's care. We also evaluated the adequacy of New Concept's accounting records, internal controls, and compliance with applicable federal, State and County fiscal guidelines governing the disbursement of foster care funds.

Summary of Findings

We identified $56,381 in excess salary compensation, $30,732 in expenditures that are not supported or inadequately supported by original receipts and $10,340 in expenditures that are unallowable because they are not program related.

In addition, we noted several deficiencies in New Concept's control over the disbursement of foster care funds. For example, we noted that New Concept needs to strengthen internal controls over mileage logs, personnel/payroll records, and bank reconciliations. Also, three primary officers of the Agency were classified as independent contractors when they should have been classified as employees of the Agency. Details of our findings are discussed in the attached report.

We have recommended that DCFS resolve the questioned costs and, if appropriate, collect all disallowed amounts. In addition, DCFS needs to ensure that New Concept's management takes the appropriate corrective actions to address the recommendations in this report. Finally, DCFS must monitor to ensure that the corrective actions taken result in permanent changes.

Review of Report

We discussed our report with New Concept's management on October 2, 2003. They have agreed to provide DCFS with a written response and corrective action plan within 30 days of the report date. 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 thank New Concept's management and staff for their cooperation during our review.

If you have any questions, please contact me, or have your staff contact DeWitt Roberts at (626) 293-1101.

JTM:DR:RL
Attachment

c: Chief Administrative Office
David E. Janssen, Chief Administrative Officer
Claudine Crank, Budget & Operations Management Branch
Department of Children and Family Services
David Sanders, Ph.D., Director
Angela Carter, Deputy Director, Bureau of Administration
Genevra Gilden, Chief, Quality Assurance Division
New Concept Group Home
Harold Trimble, Executive Director
Board of Directors
California Department of Social Services
Cora Dixon, Chief, Foster Care Audit Bureau
Sheilah Dupuy, Chief, Foster Care Rates Bureau
Public Information Office
Audit Committee
Commission for Children and Families

NEW CONCEPT GROUP HOME
REVIEW OF GROUP HOME FOSTER CARE CONTRACT

BACKGROUND

The Department of Children and Family Services (DCFS) contracts with New Concept Group Home (New Concept or Agency) to provide the basic needs and services for foster care children placed in the Agency's care. New Concept is one of two group homes licensed to operate under the corporate name of Humanistic Foundation, Incorporated. The other group home, Stockdale Boys Center, is located in Kern County. New Concept has a resident capacity of eight children. The Los Angeles County facility is located in the Second Supervisorial District.

Under the provisions of the contract, the County pays New Concept a monthly rate for each child, based on the Group Home Annual Rate determined by the California Department of Social Services (CDSS). During our review period, January 1, 2002 through December 31, 2002, the Agency received a monthly rate of $4,479 per child. During this period, the Agency received $335,084 in foster care funds from Los Angeles County.

APPLICABLE REGULATIONS AND GUIDELINES

New Concept is required to operate its Group Home in accordance with certain federal, State and County regulations and guidelines. We referred to the following applicable regulations and guidelines during our review:

- Group Home Contract, including Exhibit D, Auditor-Controller Contract Accounting and Administration Handbook (A-C Handbook)

- Federal Office of Management and Budget Circular A-122 (Circular), Cost Principles for Non-Profit Organizations

- California Department of Social Services Manual of Policies and Procedures (CDSS- MPP)

- California Code of Regulations, Title 22 (Title 22)

ALLOCATION OF COSTS

According to the A-C Handbook, contractors shall maintain a general ledger for all assets, liabilities, fund balances, revenues and expenditures. In addition, the A-C Handbook states that, if contractors provide services in addition to the services required under contract, the contractor shall allocate expenditures that benefit programs or funding sources on an equitable basis.

The Agency operates two group homes, one in Los Angeles County and one in Kern County. The Agency does not separately account for County program expenditures and does not allocate program costs between the two counties.

Although combining the funds from the counties did not affect the payments to group homes, we recommend that the Agency separately account for and allocate revenue and expenditures between its group homes. This will enable Los Angeles County to determine if its funds are spent on the Los Angeles County program.

Recommendation

1. **New Concept management develop a cost allocation plan and allocate group home expenditures between Los Angeles County and Kern County as applicable.**

REVIEW OF EXPENDITURES

Unreasonable Expenditures

New Concept incurred $56,381 in excess salary expenditures. Section 11-402 of the CDSS-MPP states that, based on the Agency's annual budget, the maximum salary amounts during 2002 for the Executive Director and Assistant Executive Director were $65,163 and $56,169, respectively. In 2002, New Concept's Executive Director was paid $97,017 or $31,854 more than the CDSS-MPP approved maximum. Also, during the same period, the Assistant Executive Director of New Concept was paid $80,696 or $24,527 more than the approved CDSS-MPP salary level. New Concept management did not provide us with an explanation to justify the higher salary levels. However, the specific amount allocable to Los Angeles County cannot be determined until New Concept management provides DCFS with their cost allocation plan. In the interim, we will question the entire excess salary amounts over the approved CDSS-MPP rates.

Unsupported/Inadequately Supported Expenditures

Per the A-C Handbook, all revenues and expenditures shall be supported by original vouchers, invoices, receipts, cancelled checks or other documentation. Unsupported expenditures will be disallowed on audit. We identified $30,732 in group home expenditures that were either not supported or the support provided was inadequate.

- $13,200 paid by the Agency to the Executive Director and the Assistant Executive Director as repayments of loans previously made to the Agency by these individuals. Although the Agency coded the amounts as reductions to loans payable in their general ledger, there are no supporting documents to indicate that loans were ever made.

- $12,690 in housekeeping expenses (approximately $1,058 per month) were incurred for the group home in Los Angeles County. The Agency did not have a contract with the contractor performing housekeeping duties. In addition, no invoices were prepared by the contractor for the services performed. Therefore, we are unable to determine whether these expenses were business related.

- $2,654 in unsupported expenditures involving payments to the Doubletree Hotel, Citibank Processing Center, Office Depot and an employee for maintenance and repairs.

- $2,188 in credit card gasoline charges to Texaco, Shell, and Exxon/Mobil that were not supported by receipts or invoices. The A-C Handbook states that all credit card disbursements must be supported by original invoices, store receipts or other external authenticating documents indicating the item purchased and the employee making the purchase. Credit card statements are not sufficient support for credit card purchases.

Unallowable Expenditures

We identified $10,340, in expenditures which are not allowable under federal and State guidelines or the County's contract. Listed below are details of these expenditures.

Vehicle Expense

Section 7 of the Circular indicates that any portion of the cost for automobiles that relates to personal use by employees (including transportation to and from work) is unallowable as a fringe benefit or indirect cost regardless of whether the cost is reported as taxable income to the employees. The Agency's Assistant Executive Director is leasing a 2002 Jaguar for which the Agency is paying the lease agreement. The lease agreement indicates that the vehicle is for personal use. Furthermore, the Assistant Executive Director stated that no mileage logs were kept to document any business use of the vehicle. During our review period, New Concept paid a total of $9,517 for costs associated with this vehicle. Specifically, the Agency paid $7,963 in auto lease payments, $1,215 in auto insurance and $339 in auto registration. We question the entire amount of $9,517 as an unallowable expense.

Alcoholic Beverages, Fines and Penalties, and Interest Payments

Sections 2, 16 and 23 of the Circular identify alcoholic beverages, fines and penalties and interest payments as unallowable costs. During our review period, New Concept spent a total of $823 on these items. Specifically, the Agency paid $92 in alcoholic beverages, $158 in parking tickets and citations, $500 to the California Department of Social Services Community Care Licensing for failure to correct a violation, and $73 in credit card finance charges and late fees. We question the entire amount expended on these items as an unallowable expense.

Recommendation

2. **DCFS management resolve the $97,453 in identified expenditures and, if appropriate, collect any disallowed amounts.**

In order to demonstrate the ability to appropriately account for foster care funds and administer the program in compliance with the terms of their agreement with the County, New Concept should implement the following recommendations:

Recommendations

New Concept management:

3. **Maintain adequate supporting documentation for all Group Home expenditures, including original itemized invoices and receipts.**

4. **Ensure that foster care funds are used only for necessary, allowable and reasonable expenditures to carry out the purpose and activities of the Group Home.**

5. **Maintain mileage logs for the 2002 Jaguar, to identify the business use of the vehicle.**

6. **Maintain appropriate documentation for all loans received / repaid by the Agency.**

Overpayments by DCFS

In January 2002, New Concept's general ledger indicated a liability of $19,296 for DCFS overpayments. Subsequently, the Agency prepared an adjusting journal entry on the advice of its CPA to remove the liability from the Agency's books. When we spoke to the Agency's CPA, the CPA did not know if the Agency had repaid DCFS for the prior years overpayments, but had decided to remove the liability because it had been on the Agency's books for a "very long time". The Agency's CEO could not provide us any documentation to show that the Agency had repaid DCFS. Therefore, DCFS management should review their payment records and meet with New Concept's management to resolve the potential overpayments.

Recommendations

7. **DCFS management resolve the $19,296 in DCFS overpayments with New Concept and, if applicable, collect any overpaid amounts.**

8. **New Concept management report payment discrepancies to DCFS in a timely manner.**

CONTRACT COMPLIANCE AND INTERNAL CONTROLS

Our review disclosed contract compliance issues and internal control weaknesses in addition to those already mentioned. DCFS must ensure that New Concept's management takes appropriate corrective actions to address each of the internal control recommendations in this report. DCFS should also monitor this contractor to ensure the corrective actions result in permanent changes.

Inadequate Accounting and Disbursement Controls

According to section A.2.4 of the A-C Handbook, a general ledger shall be maintained with accounts for all assets, liabilities, fund balances, expenditures and revenues. In addition, section A.2.0 of the A-C Handbook also indicates that postings to the general ledger and journals should be made on a monthly basis. In addition to the unsupported/inadequately expenditures mentioned previously, we also tested a sample of the invoices, receipts and cancelled checks provided by the Agency. We were unable to trace nine (15%) of 60 invoices and receipts sampled to the Agency's general ledger. It is essential that all revenue and expenditure transactions be recorded in the Agency's general ledger in order for the Agency to determine the results of its operations, financial condition, and disposition of funds paid by the County.

Recommendation

9. **New Concept management post all revenues and expenditures to its general ledger on a monthly basis.**

Payroll/Personnel Controls

New Concept's payroll and personnel procedures are not in compliance with the Circular, CDSS MPP, Title 22 and the A-C Handbook. We performed testwork to determine if New Concept has adequate controls for payroll and personnel functions. Our testwork revealed the following:

- Four (36%) of the 11 employee personnel files did not contain a salary approval sheet.

- Two (18%) of the 11 employee personnel files were unavailable for review. The Agency could not locate the personnel files for these two employees. The Agency's facility manager believes the two employees destroyed their own personnel files before leaving the facility.

- None of the 11 employee time cards were signed by their supervisor.

- None of the 11 employee benefit leave balances were properly documented. Section B.3.2 of the A-C Handbook states that employee benefit balances (e.g., sick time, vacation, personal time, etc.) should be maintained on at least a monthly basis. Benefit balances should be increased when benefit hours are earned and decreased as hours are used. The Agency's Assistant Executive Director stated that each employee receives one week of vacation time once they reach their one year anniversary. He also stated that vacation hours are tracked by reviewing time cards. However, this is not an adequate method to track benefit leave balances because it does not indicate how many hours the employees have actually accumulated or used. The Agency should prepare and maintain a benefits log to track the accumulation and usage of benefit hours as required by the A-C Handbook.

Recommendations

New Concept management:

10. **Ensure that each employee personnel files contain an authorized salary rate sheet approved by management.**

11. **Ensure that personnel files are adequately maintained with access restricted to authorized individuals.**

12. **Ensure all time cards are reviewed and approved in writing by management.**

13. **Prepare and maintain a benefits log to track the accumulation and usage of employee benefits.**

Independent Contractor Status

We noted that the three primary officers of the Agency, the Executive Director, Assistant Executive Director and the Administrator are classified as independent contractors. Section A.2.6 of the A-C Handbook states that an Agency shall ensure compliance with

Internal Revenue Service (IRS) guidelines in properly classifying employees and independent contractors. According to Internal Revenue Service (IRS) Publication 15-A, an officer of a corporation is generally considered an employee: however, an officer who performs no services or only minor services, and neither receives nor is entitled to receive any pay, is not considered an employee.

Each of the three officers received substantial compensation from the Agency for providing substantial services. Therefore, it appears that the three officers should be classified as employees and not independent contractors. New Concept should issue retroactive Wage and Earnings (W-2) forms for the three officers. In addition, DCFS management needs to ensure that no foster care funds are used by the Agency to pay for fines, penalties and interest assessed by the State Employment Development Department, Franchise Tax Board and the IRS.

Recommendations

14. **New Concept management issue retroactive Wage and Earnings (W-2) forms for the calendar years that the three officers were classified as independent contractors.**

15. **DCFS management needs to ensure that no foster care funds are used by the Agency to pay fines, penalties or interest assessed by the State Employment Development Department, Franchise Tax Board or IRS.**

Bank Reconciliations

Section 4.011 of the A-C Handbook states that bank reconciliations should be prepared within 30 days of the bank statement date and signed and dated by both the preparer and the reviewer. We reviewed the bank reconciliations for each month during 2002 and found that in seven of the twelve months no bank reconciliations were prepared. The Agency attempted to perform bank reconciliations for the other five months. However, none were signed or dated by the preparer or reviewer. Without the appropriate signatures and dates, we were unable to determine whether the bank reconciliations were prepared timely and were reviewed for appropriateness and accuracy. Bank reconciliations are necessary to verify the accuracy of the accounting records.

Recommendations

New Concept management:

16. **Prepare bank reconciliations within 30 days of the bank statement date.**

17. **Ensure bank reconciliations are reviewed and approved by management on a monthly basis and that all reconciliations are dated and signed by the preparer and reviewer.**