



July 19, 2005

The Honorable Antonio R. Villaraigosa
Mayor, City of Los Angeles
Room 303, City Hall
200 North Spring Street
Los Angeles, CA 90012

The Honorable Gloria Molina
Chair, County Board of Supervisors
500 West Temple Street, #856
Los Angeles, CA 90012

Dear Mayor Villaraigosa and Supervisor Molina:

City and County officials have raised concerns regarding Los Angeles Homeless Services Authority's (LAHSA) current fiscal condition and contract administration. LAHSA subcontractors have reported significant delays in receiving payments for services, which could jeopardize their ability to continue providing services. In addition, City and County departments who provide funding to LAHSA have noted delays in contract execution and problems with LAHSA's grant claiming process. As a result of these concerns, the General Manager of the Los Angeles City Housing Department and the County Chief Administrative Officer requested a joint City/County assessment of LAHSA's fiscal operations.

Assessment Results and Recommendations

LAHSA has a number of significant fiscal issues including the inability to pay subcontractors timely; inconsistent and untimely billings to available grant sources; and inadequate monthly and year-end financial reporting. LAHSA currently owes more than \$5 million to its service providers (64% of which is more than 30 days past due), but has less than \$700,000 in its bank account. While LAHSA recently submitted \$4.6 million in funding requests to its grantors, the agency did not submit these requests timely. These serious accounting problems have created cash flow issues for many of LAHSA's subcontractors, and raise the question of whether LAHSA can continue as the fiscal agent for publicly funded homeless services.

LAHSA management needs to take immediate action to address the Agency's billing and collection issues discussed in the attached report. LAHSA management needs to develop an appropriate allocation method for administrative costs; work with the City, County and grantors to evaluate ways to improve the Agency's contract administration functions to ensure timely execution of grants and contracts; and hire a qualified Chief Financial Officer.

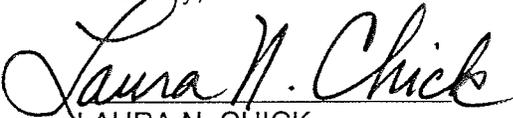
Honorable Antonio R. Villaraigosa
Honorable Gloria Molina
July 19, 2005
Page 2

Review of Report

This report was discussed with LAHSA management on July 12, 2005. LAHSA management agrees with our report and has already begun to make changes and implement our recommendations. For example, LAHSA management met with representatives from Thompson, Cobb, Bazilio, and Associates (TCBA) on July 11, 2005. The consulting firm will provide LAHSA with a formal proposal indicating how they will address LAHSA's fiscal and contracting issues. LAHSA management will concurrently begin the recruitment process for a new Chief Financial Officer. LAHSA will submit a detailed corrective action plan to your offices within 30 days of the issuance of this report.

We thank LAHSA management and staff for their cooperation and assistance during our review. City Controller and County Auditor-Controller staff will be available to meet with LAHSA and the consultants to discuss our recommendations and provide financial advice as necessary.

Sincerely,


LAURA N. CHICK
City Controller


FOR
J. TYLER McCAULEY
County Auditor-Controller

cc: Honorable Members of the Los Angeles City Council
Honorable Rockard J. Delgadillo, City Attorney
Honorable Yvonne B. Burke, Supervisor, Second District
Honorable Zev Yaroslavsky, Supervisor, Third District
Honorable Don Knabe, Supervisor, Fourth District
Honorable Michael D. Antonovich, Supervisor, Fifth District
Marcus Allen, Deputy Chief of Staff, Mayor's Office
Robert Ovrom, Deputy Mayor
Community and Economic Development
William T. Fujioka, City Administrative Officer
Mercedes Marques, General Manager, City of Los Angeles Housing Department
DeWitt Roberts, Chief Deputy Controller, City Controller's Office
David Janssen, County Chief Administrative Officer
Raymond G. Fortner, County Counsel
Carlos Jackson, Community Development Commission
William G. Vasquez, Director, Office of Community Planning and Development,
U.S. Department of Housing and Urban Development
Owen Newcomer, Chair, LAHSA Commission
Sarah Dusseault, Vice Chair, LAHSA Commission
Mitchell Netburn, Executive Director, Los Angeles Homeless Services Authority

Assessment of Current Fiscal Operations of the Los Angeles Homeless Services Authority (LAHSA)

Background

The Los Angeles Homeless Services Authority (LAHSA) was created in December 1993 as a Joint Powers Authority through an agreement between the City and County of Los Angeles. LAHSA is an independent unit of local government created to address the problems of homelessness on a regional basis. LAHSA's mission is to support, create and sustain solutions to homelessness by providing leadership, advocacy, planning and management of program funding. LAHSA is governed by a ten-member Commission, five of whom are appointed by the Mayor with the approval of City Council; and one by each of the five members of the County Board of Supervisors. The Commission sets policy and approves all contract and funding decisions for LAHSA's direct and sub-contracted operations. The Executive Director is supported by seven directors, and leads a staff of 65.

The scope and responsibility of LAHSA has grown tremendously. Starting with an initial budget of \$5 million to support five small programs, LAHSA now manages up to \$50 million annually¹. LAHSA operates two direct programs; the countywide emergency response and homeless family outreach teams, and administers approximately 200 programs through subcontracts with nonprofit agencies. As the regional coordinating agency for homeless services, LAHSA is also responsible for:

- consolidated planning and advocacy;
- coordination and linkages between programs;
- prioritization of projects for public funding;
- measurement of program effectiveness through analysis of performance outcomes and implementation of a countywide homeless management information system;
- ensuring compliance with applicable laws and regulations through fiscal and programmatic monitoring of subcontracted operations.

On June 29, 2005, City and County officials held a joint meeting to discuss additional funding/revenue sources for shelter services and governance of homeless services and administration. During the meeting, several concerns were raised regarding LAHSA's contract and fiscal performance. Some homeless shelter contractors reported to City officials that they were experiencing significant delays with contract execution and invoice payment from LAHSA. The Mayor's office and the County Chief Administrative Officer requested that a joint City-County review be conducted as soon as possible. The City Controller and County Auditor-Controller dedicated staff to perform an initial assessment.

¹ Attachment 1 presents 2005-06 budgeted sources and uses of LAHSA's funds.

**Assessment of LAHSA's Fiscal Operations
July 19, 2005**

LAHSA's Fiscal History

When LAHSA was originally created, the County of Los Angeles served as the agency's fiscal agent. All funds were held on deposit in the County treasury, and financial transactions were recorded on both LAHSA's and the County Auditor-Controller's accounting systems. LAHSA and the County Auditor-Controller worked together to allow LAHSA to attain fiscal autonomy from the County to maximize efficiency and effectiveness of both organizations. Under the direction of a new CFO, with assistance and oversight by County Auditor-Controller and other County departments, the City and County revised the Joint Powers Agreement giving LAHSA fiscal autonomy from the County in February 2001.

At that time, LAHSA's fiscal controls and procedures were functioning well. The automated accounting system was fully implemented, monthly financial statements were presented to the Commission on a regular basis, audits were up-to-date, there were no outstanding findings, controls and procedures were followed, and subcontractor invoices were processed timely.

It should be noted that a few months ago, the County Board of Supervisors, through the County Audit Committee, requested a management audit of LAHSA. Consequently, the Auditor-Controller had planned on performing a management audit of LAHSA in Fiscal Year 2005-06.

Purpose and Scope

The purpose of the assessment, which was conducted over a one-week period, was to provide an overview of LAHSA's current fiscal problems along with specific recommended actions to correct them. Our assessment consisted of interviews with LAHSA management and staff, and a review of relevant records and documents.

Assessment Results

LAHSA has a number of significant fiscal issues that must be corrected immediately if LAHSA is to continue as the fiscal agent for publicly-funded homeless services. These issues include the inability to pay subcontractor invoices timely; inconsistent and untimely billing to available grant sources; and inadequate monthly and year-end financial reporting which has prevented LAHSA from completing required audits.

As of July 8, 2005, LAHSA owes more than \$5 million to its subcontractor service providers (64% of which is more than 30 days past due), but has less than \$700,000 in its bank account. Although LAHSA has submitted \$4.6 million in funding requests to its grantors, the agency did not submit these requests timely to the City and County because of severe accounting problems. These accounting problems have created cash flow issues for many of LAHSA's subcontractors, and raise the question of whether LAHSA can continue to effectively manage its fiscal operations.

Assessment of LAHSA's Fiscal Operations

July 19, 2005

LAHSA management indicated there are several reasons for the current fiscal problems, including staff vacancies; lack of adequate direction and oversight by management; an increase in the number and restrictions of funding sources; more complicated billing procedures; an increase in the number of LAHSA programs funded by multiple grants; and the need for additional fiscal staff to handle the new programs and funding source restrictions.

The details of these and other significant issues are discussed below.

1. *LAHSA does not have procedures in place to claim grant funds and pay its subcontractors timely*

As noted earlier, LAHSA owes more than \$5 million to its subcontractor service providers, and has less than \$700,000 in its bank account. While \$4.6 million in funding requests have recently been submitted to grantors, LAHSA has not been able to timely claim all grant funds available through the City and County because of severe accounting problems.

Specifically, many of LAHSA's contracts with service providers are funded by more than one source (e.g., State and Federal funds). These multi-funded contracts require LAHSA to be able to allocate costs billed by the service providers among the various funding agencies, and ensure compliance with each funding agency's requirements. LAHSA does not have procedures in place to adequately budget and report expenditures for its multi-funded subcontracted programs. As a result:

- LAHSA is unable to process and pay invoices from service providers timely because LAHSA staff do not know which grants to charge for multi-funded programs.
- LAHSA cannot claim funds from its funding sources until the Agency has invoices to support the claimed amounts. Grants must be billed based on actual charges incurred and billed by subcontractors. Failure to claim timely has resulted in cash flow problems and delayed payments to subcontractor service providers. To allow LAHSA to make some payments to service providers, LAHSA has been using funds from other, unrelated grants to pay subcontractor expenditures when those grants cannot be billed. Federal regulations prohibit this practice. Claim cuts will result unless these errors are corrected. This matter is discussed in the next section of this report.
- LAHSA is unable to close its books for the fiscal years (FY) ended June 30, 2004 and 2005. Staff stated that many of the program expenditures incurred and invoiced by subcontractors were entered into the accounting system, but were coded to the wrong grant(s). These errors need to be corrected before LAHSA can close its books for these FYs.

Assessment of LAHSA's Fiscal Operations
July 19, 2005

Recommended Actions:

- (a) For the prior year(s) grants and subcontracts, LAHSA needs to reconcile the expenditures, billings and receipts for multi-funded programs and ensure that the grants are appropriately charged and closed out.
 - (b) LAHSA should separately identify and allocate subcontractors' budgets for each funding source upon contract execution for multi-funded programs. Subcontractors must bill in accordance with their budgets and LAHSA must record actual expenditures/billings for each funding source and program as they process invoices for payment.
2. *LAHSA does not have mechanisms in place to adequately distribute its administrative costs to grant programs.*

The lack of an appropriate method to allocate administrative costs has also contributed to LAHSA's inaccurate accounting information. For example, staff stated that they have not recorded payroll transactions for the three most recent payroll periods. This again is due to staffs' uncertainty over which grants to charge and has limited LAHSA's ability to bill their administrative costs.

In addition, LAHSA is unable to close prior-year grants because administrative costs were not appropriately allocated. This has resulted in funding overages/shortages for those grants. Staff stated that they record year-end adjustments to the accounting records in order to meet grant budgets. This practice is generally prohibited by grantors and could result in audit exceptions requiring funding to be returned to grantors.

LAHSA fiscal staff also indicated that they intended to bill their administrative costs for the current FY (2005-06) by requiring all employees to code their timecards to specific grants based on the grants' budgets, not the actual time/costs. Staff indicated this approach would be easier than having to continually make adjustments to meet grant budgets. We informed staff that charging grants based on budgets is specifically prohibited by federal cost regulations (OMB Circular A-87).

Recommended Actions:

- (a) **LAHSA must develop a new cost allocation methodology to properly distribute administrative costs to grants in accordance with federal cost principles and grant requirements.**

**Assessment of LAHSA's Fiscal Operations
July 19, 2005**

(b) LAHSA should review prior administrative expenditures billed to the agency's funding sources. LAHSA should then negotiate with grantors to adjust charges and revise contract budgets in order to close out prior year grants.

3. *LAHSA is not executing contracts with its funding agencies and subcontractors timely.*

Direct programs operated by LAHSA include the Countywide Emergency Response and Family Outreach Programs. The remainder of LAHSA's programs are operated through a number of subcontracts with nonprofit agencies throughout the community, and are funded by a variety of sources (City, County, etc.).

City-Funded Subcontracts

The City of Los Angeles' Housing Department recently voiced concern over the timeliness of LAHSA's contract execution. Specifically, all 17 of LAHSA's FY 2005-06 ESG and CDBG contracts (April 1 start date) with the City that provide funding to LAHSA have been executed. However, LAHSA has not finalized all of its contracts with its subcontractors who provide services under these City-funded contracts. Specifically, only eight of LAHSA's 46 subcontracts with agencies that provide services under City-funded contracts were executed as of June 30, 2005. LAHSA indicated that the remaining 38 contracts have been given to the subcontractors for their approval/signature. LAHSA noted that they did not receive the 17 completed contracts from the City until May 25, 2005, and did not have the authority to enter into its subcontracts until after that date.

County-Funded Subcontracts

The County's Community Development Commission (CDC) stated that all four of its FY 2005-06 contracts (July 1 start date) with LAHSA that provide County funding for LAHSA's programs had not been executed as of July 5, 2005. LAHSA staff indicated they are currently reviewing the contracts and they expect to finalize them within the next week. As a result, LAHSA subcontracts for programs to be paid by County funds have not yet been executed.

HUD Funded Subcontracts

The majority of LAHSA's subcontracts are funded directly through the federal Department of Housing and Urban Development (HUD) Supportive Housing Program (SHP). Each SHP contract must first be negotiated with HUD, and then with LAHSA and the subcontract service provider. Several providers have complained about lengthy delays in executing their SHP contracts. LAHSA management indicated that it typically takes an average of two months to

Assessment of LAHSA's Fiscal Operations
July 19, 2005

receive an executed grant agreement from HUD, although extremely complex projects may take significantly longer. However, our limited assessment did not determine the cause of these delays, including which agencies may be responsible.

Recommended Action:

LAHSA management should work with the City, County and other grantors to evaluate ways to improve the Agency's contract administration functions to ensure timely execution of grants and contracts.

- 4. *LAHSA does not have capable financial leadership with sufficient expertise to address and correct the problems.***

A primary cause of LAHSA's fiscal problems was the inadequate oversight by management, including failure on the part of the prior CFO to revise and update fiscal procedures to accommodate the growing needs of LAHSA. In addition, it appears that most of the knowledge base regarding LAHSA's overall fiscal operations was lost when the CFO resigned in May 2005.

During our assessment, we noted that staff could not always answer our questions or provide requested data. While it appears that most fiscal staff are knowledgeable in completing their assigned tasks (i.e., approve and pay invoices), they are unclear as to how these tasks fit into LAHSA's overall operations. LAHSA management noted that two of their 11 budgeted fiscal positions are vacant, and that only three of the nine existing staff have more than one year's experience at LAHSA.

It is clear that LAHSA needs capable financial leadership to direct staff on how to address the critical issues facing the agency. This is imperative to ensure the ongoing stability and integrity of LAHSA's financial operations.

Recommended Actions:

- (a) LAHSA must hire a qualified CFO to ensure the agency's fiscal operations are appropriate and in compliance with all applicable laws and regulations.**
- (b) LAHSA's new CFO should assess the organizational structure of the agency's fiscal department, including the functions and qualifications of all staff to ensure LAHSA has the capacity to function effectively.**

**LOS ANGELES HOMELESS SERVICES AUTHORITY
FISCAL YEAR 2005-06**

SOURCES:

City of Los Angeles			
LAHD: General Funds allocation	4,600,000		
LAHD: Emergency Shelter Grant Program	3,270,215		
LAHD: Community Development Block Grant	9,276,462		
<i>Total funds passed thru City contracts:</i>		17,146,677	35.3%
County of Los Angeles			
CSS: General Funds	4,005,000		
CDC: Emergency Shelter Grant Program	1,326,590		
CDC: Community Development Block Grant Program	285,000		
CDC: Independent Living Program	2,139,386		
DPSS: CalWORKS Families Project	1,900,000		
DPSS: Outreach Project	750,000		
<i>Total funds passed through County contracts:</i>		10,405,976	21.4%
State of California			
Emergency Housing and Assistance Program		146,136	0.3%
Direct Federal funding			
HUD: Supportive Housing Program	20,128,395		
FEMA: Emergency Food & Shelter Program	785,905		
<i>Total funding received directly from federal sources:</i>		20,914,300	43.0%
TOTAL SOURCES:		48,613,089	100.0%

USES:

LAHSA Direct Programs	669,151	1.4%
LAHSA Administration	3,765,040	7.7%
Sub-Contracted Programs	44,178,898	90.9%
TOTAL USES:	48,613,089	100.0%

Note: amounts and categories taken from LAHSA's FY 2005-06 Budget, adopted by LAHSA Commission on June 24, 2005.