COUNTY OF LOS ANGELES
DEPARTMENT OF AUDITOR-CONTROLLER

KENNETH HAHN HALL OF ADMINISTRATION
500 WEST TEMPLE STREET, ROOM 525
LOS ANGELES, CALIFORNIA 90012-3873
PHONE: (213) 974-8301 FAX: (213) 626-5427

WENDY L. WATANABE
AUDITOR-CONTROLLER

MARIA M. OMS
CHIEF DEPUTY

ASST. AUDITOR-CONTROLLERS

ROBERT A. DAVIS
JOHN NAIMO
JUDI E. THOMAS

December 22, 2010

TO: Supervisor Michael D. Antonovich, Mayor
Supervisor Gloria Molina
Supervisor Mark Ridley-Thomas
Supervisor Don Knabe
Supervisor Zev Yaroslavsky

FROM: Wendy L. Watanabe
Auditor-Controller

SUBJECT: **RAINBOW BRIDGE COMMUNITY SERVICES CONTRACTS REVIEW – A DEPARTMENT OF PUBLIC HEALTH HIV/AIDS CARE AND PREVENTION SERVICES PROVIDER**

We completed a fiscal review of Rainbow Bridge Community Services (Rainbow or Agency), a Department of Public Health (DPH) HIV/AIDS care and prevention services provider. The purpose of our review was to determine whether Rainbow provided the services to eligible participants and spent funds in accordance with the County contract. We also evaluated the adequacy of Rainbow's accounting records, internal controls, and compliance with the contract and applicable controls. Rainbow is located in the Third District.

At the time of our review, Rainbow had three fee-for-service contracts with DPH's Office of AIDS Programs and Policy (OAPP). OAPP paid Rainbow $514,789 from March 2008 to September 2009.

Results of Review

Overall, the areas of non-compliance noted in this review are significant and indicate that Rainbow has limited capacity to comply with their County contracts. Rainbow has difficulty meeting its financial obligations and does not have sufficient working capital to pay its bills. In addition, the Agency's most recent financial audit report for the period ended December 2008 reported that the Agency operated with negative net assets for two years and reported the Agency as a going concern.

Further, Rainbow had a number of questionable transactions and lacked sufficient internal controls over basic business processes to ensure program assets were safeguarded and that program funds were used in accordance with the County contract. Specifically, Rainbow:

- Owes $63,000 to the Internal Revenue Service and the State Employment Development Department for unpaid payroll taxes for tax years 2008 and 2009.

  Rainbow's attached response indicates that they paid some of their previous liabilities for the third quarter of 2009 and still maintain up-to-date on current obligations. They also indicate that they will conduct fundraising activities to create a reserve of $60,000 and pay down their debt.

- Paid $126,100 to Rainbow's President of their Board of Directors. The Agency indicated that the expenditures were loan repayments. However, Rainbow did not provide documentation to support the payments, such as loan agreements that identify the dates and terms of the loans and repayment plans.

  Rainbow's attached response indicates that their Board of Directors will approve future Agency loan amounts and terms of the loans.

- Did not maintain documentation, such as timecards, to support $206,961 in payroll expenditures charged to OAPP.

  Rainbow's attached response indicates they now maintain employee timecards that report time staff worked by program and personnel files that include authorized salary rates to support the Agency's payroll expenditures. In addition, the Agency provided timecards at the exit conference, however, the timecards were not for all employees sampled and the timecards did not include the number of hours worked by program.

- Incurred $8,460 in overdraft bank fees between March 2008 and September 2009 to cover the checks they issued to pay bills.

  Rainbow's attached response indicates that their goal is to have a zero tolerance of overdraft bank charges and since our audit, the charges have dropped significantly.

- Charged OAPP approximately $45,000 in rent payments made to a related party. Rainbow's residential leases consist of two properties that are owned by the Agency's President. The Agency indicated that the monthly rent amount of $5,000 per property was lower than the fair market value of leased property for the area. The contract limits lease payments to related parties to the lower of actual cost or fair market value. However, Rainbow did not provide documentation to support the fair market value or actual costs of the properties.

Rainbow's attached response indicates that the organization will provide documentation on lease amounts.

- Did not maintain double entry accounting records with a general ledger and chart of accounts. Instead, the Agency prepared a profit and loss report which included only checks and transactions that had cleared the bank account. As a result, not all disbursements were recorded and the Agency had difficulty supporting the expenditures reported on their Cost Reports.

  Rainbow's attached response indicates that they are currently maintaining the necessary accounting journals.

- Did not maintain documentation to support $1,730 in program services billed to OAPP.

  Rainbow's attached response indicates that they agree to repay the $1,730 and they have developed systems to ensure their Cost Reports are accurate, reflect the correct number of treatment days provided and that files document the clients' eligibility for services.

In addition, Rainbow lacked internal controls over basic business processes in the areas of cash, non-payroll and payroll expenditures. For example:

- The Agency's President of the Board of Directors was the only authorized check signer. He prepared and signed checks made payable to "cash" and his other businesses.

  Rainbow's attached response indicates that they designated two alternate check signers to sign checks issued to the President and his other businesses.

- The Agency made 11 checks payable to "cash" in amounts ranging from $200 to $1,500 each, totaling $9,890.

  Rainbow's attached response indicates that checks are no longer made payable to cash.

For the period reviewed, County Counsel indicated that OAPP's fee-for-service contracts did not include provisions that allowed the County to recover the questioned costs identified in this report. On March 1, 2010, OAPP amended the contract to include the appropriate language that allows the County to collect questioned costs in subsequent audits.

In addition, in July 2010, we received allegations that Rainbow reduced employees' salaries by 30%, issued inaccurate W-2s and employees were not paid due to insufficient funds. These allegations were noted in a complaint that OAPP received

which they forwarded to our office. Based on a follow-up review conducted in August 2010, we could not substantiate these allegations.

The details of our review, along with recommendations for corrective action, are attached.

Review of Report

We discussed our report with Rainbow and OAPP on May 4, 2010. In their attached response, Rainbow describes the implemented or planned corrective actions to address the recommendations in our report. We also notified DPH of the results of our review and our recommendation to terminate their contract with Rainbow.

We thank Rainbow management for their cooperation and assistance during this review. Please call me if you have any questions or your staff may contact Don Chadwick at (213) 253-0301.

WLW:MMO:JET:DC

Attachment

c: William T Fujioka, Chief Executive Officer
Jonathan E. Fielding, Director, Department of Public Health
Michael Ralke, President Board of Directors and Executive Officer, Rainbow Bridge Community Services
Public Information Office
Audit Committee

HIV/AIDS CARE AND PREVENTION SERVICES
RAINBOW BRIDGE COMMUNITY SERVICES
FISCAL YEAR 2008-09

BACKGROUND/PURPOSE

The Department of Public Health's (DPH) Office of AIDS Programs and Policy (OAPP) contracts with Rainbow Bridge Community Services (Rainbow or Agency) to provide HIV/AIDS prevention and substance abuse treatment to individuals that are at high risk of becoming infected with HIV and other communicable diseases. Rainbow also provides substance abuse residential rehabilitation and transitional housing services to individuals who are infected with HIV/AIDS and recovering from substance abuse.

The purpose of our review was to determine whether Rainbow appropriately spent funds in accordance with the County contract. We also evaluated the adequacy of the Agency's accounting records, internal controls and compliance with the County contract and applicable federal and State fiscal guidelines governing the Ryan White Comprehensive AIDS Resource Emergency Act. In addition, we determined whether the Agency provided services to eligible participants.

For the period reviewed County Counsel indicated that the OAPP HIV/AIDS fee-for-service contracts did not contain language that would allow the County to recover questioned costs as long as services were provided. Subsequent to our review, OAPP amended the payment language for new and newly renewed contracts stating that while payments are made with a fee-for-service rate, the contractor shall be reimbursed for substantiated actual costs.

FINANCIAL VIABILITY

Objective

To determine whether Rainbow is financially viable and has the ability to meet its current obligations. In addition, determine whether the Agency maintained sufficient working capital to sustain the cost of the program for at least 90 days.

Verification

We interviewed Rainbow's management and reviewed the Agency's financial records, cash flow, liabilities and earnings.

Results

Rainbow has difficulty meeting its financial obligations and did not have sufficient working capital to sustain the cost of the program for 90 days. During March 2008 to July 2009, Rainbow incurred $8,460 in overdraft bank fees because the Agency did not have sufficient cash to cover checks issued. In addition, the Agency's financial audit report for the period ending December 2008 reported that the Agency had been operating with negative net assets for two years and reported the Agency as a going concern.

The Agency also owes $63,000 to the Internal Revenue Service (IRS) and the State Employment Development Department (EDD) for unpaid payroll taxes for Tax Years 2008 and 2009 and Rainbow has no means to repay the amount. Specifically, the outstanding debt as of December 2009 was comprised of the following:

- Approximately $60,000 owed to the IRS for delinquent federal payroll taxes. The amount includes unpaid payroll taxes, penalties and interest for 2008 and 2009.
- Approximately $3,000 owed to the EDD for delinquent payroll taxes for January 2009 to September 2009.

The areas of non-compliance noted above and the remaining sections of the report are significant and indicate the Agency has limited capacity to comply with their DPH contracts. We recommend that DPH terminate their contract with Rainbow.

Recommendation

1. **DPH management terminate their contract with Rainbow.**

SERVICES BILLED/ELIGIBILITY

Objective

Determine whether the Agency provided services to individuals that meet the eligibility requirements of OAPP. In addition, determine the accuracy of the units of service billed.

Verification

We reviewed the case files for 25 program participants that received services from March 2008 to September 2009 for documentation to confirm their eligibility for OAPP services. We also traced the amount of days the Agency billed OAPP to supporting documentation.

Results

The Agency maintained documentation to support the participants' eligibility for program services. However, the Agency's daily client attendance records did not support 39 treatment days that were billed to OAPP. The undocumented billings totaled $1,730. In addition, Rainbow did not implement a fee determination system (sliding fee schedule) for participants with little or no income as required by the County contract.

Recommendations

Rainbow management:

2. **Repay OAPP $1,730 and ensure reimbursement claims accurately reflect the number of treatment days provided.**

3. **Develop a fee determination system in compliance with their County contract that has been reviewed and approved by OAPP.**

4. **Ensure that clients/participants are billed based on their ability to pay for services.**

CASH/REVENUE

Objective

Determine whether cash receipts and revenue are properly recorded in the Agency's records and deposited timely in their bank account. In addition, determine whether there are adequate controls over cash, petty cash and other liquid assets.

Verification

We interviewed Agency personnel and reviewed their financial records. We also reviewed the Agency's bank account statements from March 2008 to September 2009.

Results

Rainbow appropriately recorded and deposited OAPP payments timely. However, the Agency does not have proper controls in place to ensure County funds are accounted for and spent on reasonable and allowable expenditures. Specifically:

- The Agency did not reconcile its bank account. Bank reconciliations should be completed within 30 days of the bank statement date and reviewed and approved in writing by management.

- The Agency did not maintain a cash disbursement and cash receipt journals.

- The Agency's President of the Board of Directors was the only authorized check signer and signed checks made payable to his other businesses to repay loans.

- The Agency made payments totaling $126,100 to two businesses owned by Rainbow's President of the Board of Directors. The President and the Agency's accountant indicated the payments were to repay loans that Rainbow received from the President's other two businesses. The accountant provided cancelled checks totaling $122,800 from the other businesses made payable to Rainbow to support the loan amounts. However, the Agency did not provide documentation such as formal loan agreements that identify the terms and purpose of the loans, the total loan amounts, and the date of the loans.

- The Agency issued 11 checks payable to "cash" in amounts ranging from $200 to $1,500 each, totaling $9,890. Checks made payable to "cash" can be easily negotiated by unauthorized individuals and are more difficult to control and support. According to the Agency, the checks were used to obtain cash to pay vendors that

refused to accept Rainbow's business checks due to previous Non-Sufficient Funds checks that they received. We reviewed the documentation for six of the 11 checks and confirmed the expenditures were appropriately documented.

Recommendations

Rainbow management:

5. **Reconcile the Agency's bank account within 30 days of the bank statement date and ensure the reconciliation is reviewed and approved in writing by management.**

6. **Maintain a cash disbursement and cash receipt journals.**

7. **Require Rainbow's Board of Directors to designate an alternate check signer, to sign any check issued to the Board's President.**

8. **Discontinue issuing checks to "cash".**

9. **Document the terms and agreement of all outstanding and future loans made to the Agency, and ensure the agreement is approved by the Agency's Board of Directors.**

COST ALLOCATION PLAN

Objective

Determine whether the Agency's Cost Allocation Plan was prepared in accordance with the County contract and use to appropriately allocate shared program expenditures.

Verification

We reviewed Rainbow's Cost Allocation Plan and accounting records that reported financial activity from March 2008 to September 2009.

Results

Rainbow's Cost Allocation Plan was not in compliance with the contract. The Cost Allocation Plan used budgeted units of service and not actual units of service as the basis for allocating Rainbow's expenditures among its programs.

Additionally, Rainbow did not maintain an accounting system to record all financial transactions in accordance with the County contract. Specifically, Rainbow:

- Did not maintain double entry accounting records with a general ledger and a chart of accounts. Instead, the Agency prepared a profit and loss report which included only

checks and transactions that had cleared the bank account. As a result, not all disbursements were recorded.

- Did not establish separate cost centers for its various programs.
- Did not provide documentation to support the allocated program costs reported on their Cost Reports.

Recommendations

Rainbow management:

10. **Ensure that cost allocations are based on actual data.**
11. **Maintain double entry accounting records with a general ledger and the necessary subsidiary ledgers for recording and summarizing all financial transactions for the OAPP Program.**
12. **Establish a chart of accounts for classifying transactions by program and activity.**
13. **Maintain documentation to support expenditures allocated to the OAPP Program.**

EXPENDITURES

Objective

Determine whether program expenditures are allowable under the County contract, properly documented and accurately billed to the program.

Verification

We interviewed Agency personnel, reviewed financial records and documentation for 27 non-payroll expenditure transactions totaling $37,957.

Results

Rainbow did not provide documentation to support $5,570 (15%) of the $37,957 sampled. Specifically, Rainbow did not provide:

- A valid service agreement for $2,000 paid to a consultant and the invoice submitted by the consultant did not identify the services provided, date of service or hours spent on program activities.
- Support for payments totaling $3,570 for food and supplies.

In addition, the Agency charged OAPP approximately $45,000 in rent payments made to a related party. Rainbow's residential leases consist of two properties that are owned by the Agency's President. The County contract requires Agencies to comply with the Office of Management and Budget (OMB) Circular A-122 which only allows Agencies to claim the lesser of actual costs or fair market value for related party transactions. Rainbow did not provide documentation to support the rent payments for these properties.

We are not recommending that Rainbow repay the unsupported expenditures above because the OAPP HIV/AIDS fee-for-service contracts in question did not contain language that would allow the County to recover questioned costs.

Recommendations

Rainbow management:

14. **Maintain supporting documentation for all program expenditures, including vendor invoices, receipts and contracts.**

15. **Provide documentation to determine the lease amounts are in compliance with the provisions in OMB Circular A-122.**

FIXED ASSETS AND EQUIPMENT

Objective

Determine whether the Agency's fixed assets and equipment purchases made with OAPP funds are used for the OAPP Program and are safeguarded.

We did not perform test work in this area, as the Agency did not charge OAPP any costs for the purchase of any fixed assets.

Recommendation

None.

PAYROLL AND PERSONNEL

Objective

Determine whether payroll is appropriately charged to the program. In addition, determine whether personnel files are maintained as required.

Verification

We traced payroll expenditures to the Agency-wide payroll register. We also reviewed the personnel files for ten employees that were charged to the OAPP Program.

Results

Rainbow does not have proper payroll controls in place to ensure payroll expenditures are authorized and accurate as required by their fee-for-service contract. Specifically, the Agency's payroll costs of $206,961 were not supported by timecards. In addition, authorized salary rates were not maintained in the personnel files for the ten employees sampled.

As stated above, although we are questioning the $206,961 in unsupported payroll costs, we are not recommending that Rainbow repay OAPP because based on County Counsel the OAPP HIV/AIDS fee-for-service contracts did not contain language that would allow the County to recover questioned costs as long as services were provided.

Recommendations

Rainbow management ensure:

16. **Payroll expenditures are supported by employee time records or timecards.**

17. **All employee personnel files contain current authorized salary rates.**

COST REPORTS

Objective

Determine whether the Agency's Cost Reports reconcile to the Agency's financial accounting records.

Verification

We traced the Agency's general ledger to the Agency's Cost Reports submitted to OAPP for the period ended February 2009 and June 2009.

Results

The Agency's accounting records did not support the amounts reported on the Agency's Cost Reports. As stated earlier in our report, Rainbow did not identify OAPP related expenditures separately in their financial records. The Agency also could not explain or provide any documentation to support their amounts reported on their Cost Reports for their three OAPP contracts.

Recommendations

Refer to Recommendations 11, 12, 13, 14 and 17.

ALLEGATIONS

Objective

Determine if allegations received in July 2010 from OAPP can be substantiated. OAPP received allegations that Rainbow management reduced employees' salaries by 30%, issued inaccurate W-2s to employees and payroll checks issued to employees were returned due to insufficient funds and were not reissued.

Verification

In August 2010, we interviewed the Program Director and two of his employees who were employed by Rainbow at the time the allegations were made and were still employed at the time of our review.

Results

Based on the interviews of the Agency's three employees, the complaints were not substantiated. Specifically:

- Two of three employees stated that they received a W-2 for 2009 from the Agency and that the salary amount reported was accurate. The third employee was hired in 2010 therefore, did not receive a W-2 for 2009.

- All three employees indicated that their salaries had not been decreased by the Agency.

- All three employees stated that they had not experienced any problems cashing Rainbow's payroll checks. One employee indicated that the Agency told him once to wait one to two days before cashing a check.

As a result of our interviews, it appears that Agency employees are being paid and according to their authorized salary rate. In addition, employees received correct W-2s for 2009. However, due to the Agency's financial condition, the Agency may not always have sufficient funds to pay for their employees and has, on occasion, asked staff to wait before cashing checks.

Recommendation

Refer to Recommendation 2.

To: Maria McGloin
Program Specialist III

From: Michael Ralke
Rainbow Bridge Community Services

Date: June 10, 2010

Re: Rainbow Bridge Community Services Contracts Review – A Department of Public Health HIV/Aids Care and Prevention Services Provider

The Purpose of this letter is to follow-up from a meeting held in your department last month with you. We were asked to respond in writing to the draft report dated March xx, 2010.

The following should address each major area.

1. **Financial Viability**

The Agency has been able to maintain federal and state payroll tax payment on time and has paid some of the previous liabilities of third quarter 2009.

- Our goal is to have a zero tolerance of overdraft bank charges. Since the audit through May 5, 2010, the charges have dropped significantly to a total of $261.00. This is 3% of the total from the audit report.

Plan: To meet our ongoing obligations and develop and sustain other ongoing revenue streams to meet future unforeseen obligations and retire any previous Agency debt.

2. **Services Billed / Eligibility**

Redundancy systems have been developed to ensure that reimbursement claims are accurate and reflect the correct numbers of treatment days provided; and that all clients provide appropriate documentation to determine eligibility for program services.

- The Agency's fee system has been submitted to OAPP and is currently under review.

2526 Hyperion Avenue, Suite 4 • Los Angeles, CA 90027 • 323-671-1600 • Fax: 323-671-1605 •
www.rainbowbridgecommunityservices.org

3. **Cash / Revenue**

- The Agency now reconciles its bank account within 30 days, and is reviewed and approved by the Treasurer of the Board.
- A cash disbursement system has been implemented and is adhered to.
- The Board of Directors has designated two alternate check signers.
- Checks are no longer issued to cash.
- Loans to the Agency will be approved by the Board of Directors as to terms and amounts accepted.

4. **Cost Allocation Plan**

- A cost allocation plan has been developed and has been reviewed by OAPP staff.
- Agency is now utilizing QuickBooks and has accounts in the general ledger and subsidiary accounts.
- A chart of accounts has been developed.
- All expenditures are now allocated to the OAPP program with supporting documentation.

5. **Expenditures**

- The organization maintains documentation of all program expenditures, including vendor invoices, receipts and contracts.
- Agency will provide documentation on lease amounts to show compliance with provisions in OMB A-122.

6. **Fixed Assets and Equipment**

No findings

7. **Payroll & Personnel**

- All employees submit time cards, which are approved by supervisor. The cards also allocate time according to cost centers.
- All personnel files now contain current authorized salary rates.
- Note – Agency located time cards from the audit period which were stored, and subsequently showed them to staff.

8. **Cost Reports**

- Agency costs are currently allocated based on actual data, according to acceptable accounting standards, i.e. general ledger and journal, and chart of accounts.

Supporting documents have been provided to staff to show our progress in the preceding areas.

Time cards; chart of accounts; profit/loss by class; pay rate summary of employees; general ledger; state and federal tax deposit receipts; and bank charges to May 2010 were all provided to staff to support the Agencies progress in becoming fiscally sound.

The Board has met to discuss these issues and is prepared over the next nine months to ensure the Agency's sustainability is achieved.

cc: Jackie Montero, OAPP

2526 Hyperion Avenue, Suite 4 • Los Angeles, CA 90027 • 323-671-1600 • Fax: 323-671-1605 •
www.rainbowbridgecommunityservices.org

To: Maria McGloin
Program Specialist III

From: Michael Ralke
Rainbow Bridge Community Services

Date: June 24, 2010

Re: Rainbow Bridge Community Services Contracts Review – A Department of Public Health HIV/Aids Care and Prevention Services Provider

Addendum to Response Dated June 10, 2010

1. **Financial Viability**

The Board has recently met and knows the challenge we must put forth to raise money thru a variety of fundraisers over the next few months to create a reserve of $60,000 and to pay down outstanding debt.

With current funding levels we are able to maintain all ongoing or current obligations.

If by early 2011, we have not created a sizable reserve and attacked our debts, the Board knows that the options are a joint venture or merger with a larger non-profit.

Initial discussions have been made with a couple of non-profits with $5 million to $25 million annual budgets, both of which are interested in such mergers. Assuming and retiring any RBCS debt are part of those discussions.

2. **Repayment of $1,730.00**

Rainbow Bridge Community Services, Inc. agrees to repay the amount of $1,730.00.

This was mostly for services from our Day Treatment Program which the Agency no longer provides. The documentation was missing from some Day Treatment visits in 2008.

cc: Jackie Montero, OAPP

2526 Hyperion Avenue, Suite 4 • Los Angeles, CA 90027 • 323-671-1600 • Fax: 323-671-1605 •
www.rainbowbridgecommunityservices.org