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February 27, 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: **FISCAL REVIEW OF INTERNATIONAL FOSTER FAMILY AGENCY – A FOSTER FAMILY AGENCY FOSTER CARE CONTRACTOR**

Attached is our audit report on International Foster Family Agency (International) fiscal operations for the period July 1, 2000 through June 30, 2001. International is licensed to operate a Foster Family Agency (FFA) and, for the period of our review, had 384 children placed in 189 certified homes. During our review period, International received $5,286,572 from Los Angeles County and $1,389,612 from San Bernardino and Riverside Counties in foster care funds. International paid $2,731,727 of this amount directly to foster parents. The Agency's administrative office is located in the Second Supervisorial District.

As a result of the findings from this review period, we have initiated a financial review of International's fiscal operations for FY 2001-02.

Scope

The purpose of our review was to ensure that International 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 International's accounting records, internal controls, and compliance with applicable federal, State and County fiscal guidelines governing the disbursement of FFA foster care funds.

Summary of Findings

Our review disclosed $320,155 in questioned costs. Included in the questioned costs are $103,359 in unreasonable expenditures, $114,177 in expenditures that are unallowable because they are not program related, and $102,619 in expenditures that were not supported or inadequately supported by original receipts.

In addition, we noted several deficiencies in International's controls over the receipt and disbursement of foster care funds that contributed to the questioned amounts discussed above. We also noted that International needs to strengthen internal controls over fixed assets, personnel/payroll records, bank reconciliations, foster parent agreements and payment discrepancies. 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 must ensure that International'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 International's management on February 13, 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 International's management and staff for their cooperation during our review.

JTM:DR:RL
Attachment

cc: David E. Janssen, Chief Administrative Officer
Department of Children and Family Services
Marjorie Kelly, Interim Director
John Oppenheim, Chief Deputy Director
Paul Freedlund, Bureau Chief of Finance and Administration
Genevra Gilden, Chief, Quality Assurance Division
International Foster Family Agency
Betty Jones, Interim Chief Executive Officer
Board of Directors
California Department of Social Services
Sharon Ferrante, Chief, Foster Care Audit Bureau
Evelyn Hemenover, Chief, Foster Care Rates Bureau
Public Information Office
Audit Committee
Commission for Children and Families

INTERNATIONAL FOSTER FAMILY AGENCY
FISCAL REVIEW OF FOSTER FAMILY AGENCY CONTRACT

BACKGROUND

The Department of Children and Family Services (DCFS) contracts with International Foster Family Agency (International or Agency), as a Foster Family Agency (FFA), to recruit, certify, train and support foster family homes and to provide treatment and support services for DCFS children placed in these homes. During our review period of July 1, 2000 through June 30, 2001, International placed 384 children in 189 certified homes. International's administrative office is located in the Second Supervisorial District.

Under the provisions of the contract, the County pays International a monthly rate for each child, based on the FFA Annual Treatment Rate Notification Letter determined by the California Department of Social Services (CDSS). For our review period, International received a monthly rate between $1,467 and $1,759 per foster child and the Agency received $5,286,572 in FFA funds from Los Angeles County.

CDSS has also established minimum amounts the FFA is required to pay certified foster parents. Effective January 1, 2000, the FFA is required to pay a minimum monthly rate of $578 to $753 per child, based on the age of the child. During the period of our review, International paid a total of $2,731,727 to foster parents.

APPLICABLE REGULATIONS AND GUIDELINES

International is required to operate its FFA in accordance with certain federal, State and County regulations and guidelines. We referred to the following applicable regulations and guidelines during our audit:

- FFA Contract, including Exhibit F, 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).

Summary of Findings

Our review disclosed $320,155 in questioned costs. Included in the questioned costs are $103,359 in unreasonable expenditures, $114,177 in expenditures that are unallowable because they are not program related, and $102,619 in expenditures that were not supported or inadequately supported by original receipts.

In addition, we noted several deficiencies in International's controls over the receipt and disbursement of foster care funds that contributed to the questioned amounts discussed above. We also noted that International needs to strengthen internal controls over fixed assets, personnel/payroll records, bank reconciliations, foster parent agreements and payment discrepancies.

ALLOCATION OF COSTS

In addition to Los Angeles County, International also administers FFA programs for San Bernardino and Riverside Counties. International received a total of $6,676,184 in FFA funding from the three counties, $5,286,572 from Los Angeles County and an additional $1,389,612 from San Bernardino and Riverside Counties.

During our review, we noted that the Agency does not allocate program costs between the three counties. Although combining the funds from these counties does not affect the payment to the individual foster parents, it is recommended that the Agency allocate the expenditures between the different counties' FFA programs. By allocating their costs, International can match their expenditures to the appropriate program revenues.

Recommendation

1. **International management develop a cost allocation plan and allocate expenditures between the Los Angeles, San Bernardino and Riverside Counties' FFA programs as applicable.**

QUESTIONED COSTS

Our review disclosed a total of $320,155 in questioned costs. We divided the questioned costs into three categories: Unreasonable Expenditures, Unallowable Costs and Unsupported/Inadequately Supported Costs. Details of these costs are discussed below.

Unreasonable Expenditures

International incurred $103,359 in expenditures that were unreasonable in providing care and services to foster children placed by the Agency.

Salary Compensation

On September 19, 2002, International's Board of Directors terminated its Chief Executive Officer (CEO). However, during our review period, International paid its

former CEO $227,544 in compensation. Neither the State nor the County has guidelines, specific to FFAs that establishes annual salary limits for CEOs. However, the A-C Handbook allows only those expenditures that are necessary, proper and reasonable to carry out the purpose and activities of the program.

We reviewed the salary paid to CEOs of three similar sized FFAs audited by the Auditor-Controller's office in the past two years and noted that the average annual salary for FFA executive officers is approximately $142,000. In addition, a national survey conducted by *"The Non Profit Times"* for nonprofit organizations generating revenues between $1 million and $9.9 million indicated that the average salary for CEOs during calendar year 2000 was $80,351. For calendar year 2002 the average CEO salary increased to only $86,759.

As a result, we are questioning $85,544 of the CEO's salary; the difference between the average CEO's salary for the three similar FFAs and International's former CEO's compensation.

Transportation Costs

International's CEO leased a 1999 Cadillac Seville for $28,456 and incurred an additional $2,589 in auto maintenance and repairs related to this vehicle. To determine the business usage of the vehicle, we reviewed the mileage log. The CEO's mileage log did not show the odometer readings of the vehicle but did indicate the date, destination, nature of the trip and miles driven. During FY 2000-01, the CEO traveled 14,251 miles for business related purposes. Based on this information, we projected the total business miles since April 1999 (when the vehicle was first leased) would be about 43,000. However, the odometer reading of the vehicle on March 25, 2002 was 61,195 miles, indicating that the vehicle was also used about 30% of the time for personal purposes. A further inquiry confirmed that the former CEO utilized the vehicle for personal business.

Section 7(g) of the Circular states that the cost of organization-furnished automobiles that relates to personal use by employees (including transportation to and from work) is unallowable. In addition, the A-C Handbook states that only those expenditures that are necessary, proper and reasonable to carry out the purposes of the program are allowable. A Cadillac Seville is a luxury vehicle and it was purchased primarily to benefit International's CEO. It is not reasonable or necessary for the Agency to use public funds on a luxury vehicle.

To determine a reasonable amount for vehicle expense, we utilized the amount paid to a County Department Head, $525 per month, as a standard. Therefore, we question $17,815 of the vehicle expense, $12,145 as excessive and unreasonable and $5,670 for non-business use of the vehicle.

Unallowable Costs

We identified $114,177 in unallowable FFA expenditures. Listed below are the details of these expenditures.

Bad Debts

The former CEO of International stated that the Agency used FFA funds to assist foster parents in obtaining homes under the Federal Housing and Urban Development (HUD) program. The project failed and the Agency incurred losses. As a result, International wrote off, as a bad debt expense, notes receivable totaling $80,000. According to Attachment B, Selected Items of Cost, Number 3 of the Circular, bad debts, including losses (whether actual or estimated) arising from uncollectible accounts and other claims, related collection costs, and related legal costs, are unallowable.

Leasehold Improvements

International spent $21,680 for leasehold improvements to their Carson facility. Costs incurred for necessary maintenance, repair, or upkeep of buildings and equipment, which do not add to the permanent value of the property nor appreciably prolong its intended life but keep it in an efficient operating condition, are allowable under State and federal guidelines. However, International used these funds for framing/drywalls, doors, carpet and electrical installation to their leased facility. Per the Circular, Section 15(d), capital expenditures for improvements to land, buildings, or equipment, which materially increase their value or useful life, are unallowable as a direct cost except with the prior approval of the awarding agency. International could not provide documentation showing DCFS approved the building improvements. Therefore, these costs are unallowable.

Interest, Penalties and Other Unallowable Costs

International used FFA funds on unallowable costs totaling $10,892. The unallowable costs consist of $10,096 in interest expense on loans from Bank of America, $75 from over limit fees, and $110 for late payment fees. In addition, we found expenditures of $611 in miscellaneous finance charges. According to the Circular, section 23(a), the costs incurred for interest on borrowed capital or temporary use of endowment funds, however represented, are unallowable. Section 16 of the Circular also indicates that fines and penalties are strictly unallowable.

Investment Advisory Fees

International had an investment account with Solomon Smith Barney. On July 1, 2000, the investment account's balance was $107,437. As of June 30, 2001, the balance was $111,316. International closed this account on February 12, 2002 due to the downturn of the stock market and transferred the balance of $113,880 to the Agency's Bank of America account. However, International incurred $1,605 in investment and advisory service fees. According to the Circular, section 23(c), costs of investment counsel and

staff and similar expenses incurred solely to enhance income from investments are unallowable.

Unsupported/Inadequately Supported Costs

A-C Handbook states that original vouchers, invoices, receipts, or other documentation shall support all revenues and expenditures. Unsupported expenditures will be disallowed on audit. We identified $102,619 in FFA expenditures that were either not supported or the support provided was inadequate.

- $65,697 in credit card payments for items such as clothing, travel, car rentals, gas purchases, vehicle maintenance charges, meals, toys, cell phones, office supplies, flowers, and movie tickets. The credit card purchases reviewed were missing necessary documentation such as itemized receipts, the name of the person for whom the expense was incurred or the purpose of the expense.

- $18,746 of additional expenditures involving petty cash reimbursements, mileage reimbursements, clothing, telephone, and training that were not supported or adequately supported by receipts or invoices.

- $12,970 in checks paid to the CEO. The Agency did not provide adequate documentation for purchases involving such items as computers, travel expenses, auto repairs, parking fees, recreational activities, furniture and clothing.

- $3,821 in life insurance payments to Petersen International Underwriters, United States Life and Transamerica Occidental during our audit period. Per the Circular, costs of insurance on the lives of trustees, officers, or other employees holding positions of similar responsibility are allowable only to the extent that the insurance represents additional compensation. However, the costs of such insurance, when the organization is named as beneficiary, are unallowable. We requested copies of the Agency's life insurance policies, but the Agency did not provide us with copies of the documents.

- A $1,385 payment to an independent contractor, for which International did not provide an invoice identifying work performed, hours worked or the rate charged.

Recommendations

2. **DCFS management resolve the $320,155 in unreasonable expenditures, unallowable costs, unsupported / inadequately supported costs and, where appropriate, collect any disallowed amounts.**

International management:

3. **Refrain from purchasing expensive vehicles.**

4. **Maintain detailed vehicle mileage logs, including the odometer readings for all Agency vehicles.**

5. **Ensure that FFA funds are used only for necessary, allowable and reasonable expenditures to carry out the purpose and activities of the Agency.**

6. **Maintain adequate supporting documentation for all FFA expenditures, including original itemized invoices and receipts.**

DCFS OVERPAYMENTS

As of June 30, 2001, International's unaudited financial statements indicated $119,395 "Due to LA County for Overpayments." International converted $67,615 of the payables to revenues. International's Controller told us that the $67,615 represented DCFS overpayments from 1998 and 1999. These monies should not have been converted to revenues; instead, International should have notified DCFS of the overpayment, initiated a review of these payables and reconciled their financial records with DCFS. (International informed us that a portion of these overpayments were also due to Riverside and San Bernardino Counties.)

Recommendations

7. **DCFS management work with International to resolve the overpayments and, where appropriate, collect any disallowed amounts.**

International management:

8. **Work with Los Angeles County and the other Counties to investigate and resolve the $119,395 of overpayments to various Counties and establish repayment plans as needed.**

9. **Report payment discrepancies to DCFS in a timely manner.**

CONTRACT COMPLIANCE AND INTERNAL CONTROLS

We noted a number of contract compliance issues and internal control weaknesses in addition to those already mentioned. These deficiencies contributed to the inappropriate or undocumented expenditures discussed above. DCFS must monitor to ensure that International's management takes appropriate corrective actions to address each of these deficiencies and that the corrective actions result in permanent changes.

Revenue and Disbursement Procedures

The A-C Handbook states that cash receipts (i.e., cash or checks) totaling $500 or more shall be deposited within one day of receipt. Collections of less than $500 may be held and secured and deposited weekly or when the total reaches $500, whichever

comes first. Our review disclosed that International frequently deposited DCFS warrants from five to seven days from the date of receipt. On one occasion, International deposited warrants totaling $277,231 seven days after receipt.

We also noted several instances where only one signature, the CEO's, was on checks. Normally, the agency has two signatures for each check. To ensure that disbursements are appropriate, the Agency should establish a written policy to require two signatures on checks issued above a specified amount (e.g., $500).

Recommendations

10. **International management ensure cash receipts totaling $500 or more are deposited within one day of receipt.**

11. **International management establish a written policy to require two signatures on checks issued for amounts over an established amount.**

General Accounting Procedures

We reviewed International's accounting procedures and noted the following:

- International's Schedule of Fixed Assets as of June 30, 2001 includes a schedule of all assets greater than $1,000. However, we noted that the Total Depreciation, Total Fixed Asset and Accumulated Depreciation amounts indicated on the schedule does not match the amounts reported on the Agency's financial statements. International's Controller stated that she did not believe the schedule was accurate. The A-C Handbook states that each contractor shall maintain a current listing of its fixed assets.

- The Agency's most recent physical inventory sheet was dated September 1999. The A-C Handbook states that an inventory of all fixed assets should be performed, at least annually, to ensure that all fixed assets are accounted for and maintained in proper working order.

- International's accounting did not include interest income from a CD account with Bank of America for the months of April and May 2001. The unrecorded interest income totaled $1,083 ($568 in April 2001 and $515 in May 2001).

Recommendations

International management:

12. **Ensure that the Agency's Schedule of Fixed Assets is accurate and that the calculated depreciation expense, accumulated depreciation and total asset amounts agree to the agency's financial statements.**

13. **Perform a physical inventory of all fixed assets, at least annually, to ensure that the fixed assets are accounted for and maintained in proper working order.**

14. **Ensure all interest income is properly recorded on the general ledger.**

Foster Parent Payments

We sampled 15 foster parent payments involving 53 foster children and found the following:

- One payment did not meet the State mandated minimum. The payment to a certified foster family totaled $395. However, the State requirement for a child of this age was $595. Therefore, International underpaid the foster family $200 for the child's care.

- Two (4%) of 53 agreements did not contain a payment rate for the provision of care for the foster child. The Agency needs to ensure that the payment rate is listed on the foster parent agreement.

- Five (9%) of 53 agreements where the foster child's date of birth (DOB) is different from the DOB that appears on the payment information. The Agency needs to ensure that all children's DOB is accurate and properly documented since the payment rates are based on the child's age.

Recommendations

International's management:

15. **Pay $200 in foster parent underpayments and ensure that foster parents are paid appropriately and in accordance with the minimum rates established by the CDSS.**

16. **Ensure that foster parent agreements contain current and accurate information including the payment rate and date of birth for each child.**

Payroll/Personnel Controls

International's payroll and personnel procedures are not in compliance with the Circular, CDSS MPP, Title 22 and the A-C Handbook. We sampled 14 employees and found the following:

- For two (14%) of 14 employee personnel files reviewed, the authorized salary amount/rate did not agree to the amount paid to the employee. CDSS MPP Section 11-402 requires that supporting documentation be maintained for all program expenditures, including employee salary rates.

- One (7%) of 14 employee timecards reviewed was not signed by a supervisor. This timecard belongs to the CEO who does not have a direct supervisor and, therefore, her timecard was never reviewed. The Agency should have a member of the Board of Directors who is not considered an "interested person" as defined in California Corporations Code Section 5227, review and approve the CEO's timecard.

Without proper payroll and personnel controls in place, the Agency cannot ensure payroll expenditures are authorized or accurate.

Recommendations

International management:

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

18. **Ensure that the CEO's timecard is reviewed and signed by a member of the Board of Directors who is not considered an "interested person" as defined in California Corporations Code Section 5227.**

Bank Reconciliations

A-C Handbook Section 4.011 states that monthly bank reconciliations should be prepared within 30 days of the bank statement date and signed and dated by both the preparer and the reviewer. At International, bank reconciliation's are not signed and dated by the preparer. We reviewed the bank reconciliations for the months of July 2000 through June 2001 and noted only the initials of the former CEO and various pencil marks. Therefore, we were unable to determine whether the bank reconciliations were prepared timely and reviewed for appropriateness and accuracy by management.

Recommendation

19. **International management ensure the Agency's bank reconciliations are reviewed by a supervisor and approved (signed and dated) in writing for appropriateness and accuracy.**