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

FROM: J. Tyler McCauley
Auditor-Controller

SUBJECT: **FISCAL REVIEW OF CLEO'S GROUP HOME - A GROUP HOME FOSTER CARE CONTRACTOR**

Attached is our audit report on Cleo's Group Home (CGH or Agency) fiscal operations for July 1, 2004 through June 30, 2005. The Department of Children and Family Services (DCFS) contracted with CGH to operate a group home (GH) with a resident capacity of six children. CGH is located in the Second Supervisorial District.

During our review period, DCFS paid CGH a monthly rate of $4,102 per child based on a rate determined by the California State Department of Social Services (CDSS). During the review period, CGH received a total of $237,933 in GH foster care funds from DCFS. DCFS did not renew CGH's contract when it expired on October 31, 2006.

Scope

Our review was intended to determine whether CGH complied with its contract terms and appropriately accounted for and spent foster care funds on allowable and reasonable expenditures. We also evaluated the adequacy of CGH's accounting records, internal controls and compliance with applicable federal, State and County fiscal guidelines governing the disbursement of GH foster care funds.

Summary of Findings

We identified $89,081 in questioned costs and $2,598 in potential overpayments from DCFS. In addition, we noted that CGH failed to maintain workers' compensation insurance for its employees and did not have audited financial statements. CGH also needs to pay delinquent payroll taxes owed to the Internal Revenue Service and strengthen its internal controls over disbursements, payroll and bank reconciliations.

We have recommended that DCFS resolve the questioned costs and, to the extent possible, pursue the collection of disallowed amounts. In addition, DCFS needs to ensure that, if they consider contracting with CGH in the future, CGH management takes action to address the recommendations in this report, and monitor to ensure that the corrective action results in permanent changes.

Subsequent Events

As noted earlier, DCFS did not renew CGH's contract after it expired in October 2006. DCFS advised us that CGH was placed on "Do Not Use" status, and all DCFS children were removed from the agency.

Review of Report

We discussed our report with CGH management on October 10, 2006. The Agency will provide their response to our report directly to DCFS. DCFS will incorporate the Agency's response into a Fiscal Corrective Action Plan that will be submitted directly to the Board of Supervisors. We thank CGH management and staff for their cooperation during our review.

Please call if you have any questions, or your staff may contact Jim Schneiderman at (626) 293-1101.

JTM:MO:JLS:MM

Attachment

c: David E. Janssen, Chief Administrative Officer
Patricia S. Ploehn, Director, Department of Children and Family Services
Cleo's Group Home
Norlon Davis, Executive Director
Board of Directors
California Department of Social Services
Cora Dixon, Bureau Chief, Foster Care Audits Bureau
Sheliah Dupuy, Bureau Chief, Foster Care Rates Bureau
Public Information Office
Audit Committee
Commission for Children and Families

CLEO'S GROUP HOME
FISCAL REVIEW

REVIEW OF EXPENDITURES

We Identified $89,081 in questioned costs and $2,598 in overpayments. Details of these costs/revenues are discussed below.

Applicable Regulations and Guidelines

CGH is required to operate its GH in accordance with the following federal, State and County regulations and guidelines:

- GH Contract, including Exhibit C-1, Auditor-Controller Contract Accounting and Administration Handbook (A-C 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)

Unallowable Costs

We identified $271 in unallowable expenditures, as follows:

- $192 in penalties, $152 in late payment fees and $40 in non-sufficient fund bank account fees. Penalty payments are not allowable under Circular Section 16.
- $79 in petty cash expenditures that appear personal in nature and not for the group home children's benefit for items such as, an adult priced movie ticket, grooming fees for a pet even though the Agency does not have a pet, and women's garments, although the Agency is an all boy's facility. The Section 1.5 of the A-C Handbook states that only those expenditures that are necessary, proper and reasonable to carry out the purposes and activities of the program are allowable.

Unsupported/Inadequately Supported Costs

The A-C Handbook, Section A.3.2 states that all revenues and expenditures shall be supported by original invoices, receipts, or other supporting documents, and that unsupported expenditures will be disallowed upon audit.

We identified $88,810 in group home expenditures that were either unsupported or inadequately supported. Specifically:

- $36,574 in unsupported salary payments made to seven Agency employees, pay to the Executive Director for training in addition to regular salary payments and a cash advance to an Agency employee.

- $19,971 in inadequately supported expenditures for which the Agency only provided cancelled checks as support for the expenditures. These inadequately supported expenditures were for items such as insurance, training, credit card purchases, cell phone bills, electronics, groceries and utilities.

- $20,193 in unsupported petty cash expenditures. The Executive Director received $24,844 in petty cash reimbursements during our review period. However, CGH was only able to provide documentation supporting $4,650.

- $9,921 in payments for vehicle lease payments, gasoline and other vehicle related expenditures. CGH did not maintain mileage records, or other documentation indicating that these expenses benefited the group home children.

- $2,091 of the $4,650 in documented petty cash expenditures, cited above, were inadequately supported because there was no documentation of the purpose or recipient of the purchased item(s). As a result, we could not determine if the expenditures benefited the group home children.

- $60 in petty cash expenditures that were expensed for more than their actual receipt amounts.

Recommendations

1. **DCFS management resolve the $89,081 in questioned costs and, to the extent possible, collect any disallowed amounts.**

2. **If DCFS considers contracting with CGH in the future, DCFS should ensure that CGH management consistently maintains adequate supporting documentation for all foster care expenditures, including original itemized receipts/invoices and mileage logs.**

OVERPAYMENTS BY DCFS

We reviewed 65 payment records for six group home children and noted one with an overpayment of $2,598 from DCFS. DCFS management should work with CGH management to validate the $2,598 overpayment and, if appropriate, collect the overpayment. If DCFS considers contracting with CGH in the future, CGH management should ensure that any future payment discrepancies are immediately reported to DCFS, and any overpayments are repaid promptly.

Recommendations

3. **DCFS management Work with CGH management to validate the $2,598 overpayment and, if appropriate, collect the overpayment.**

4. **If DCFS considers contracting with CGH in the future, CGH management should ensure that any future payment discrepancies are immediately reported to DCFS and any overpayments are repaid promptly.**

DELINQUENT PAYROLL TAX PAYMENTS

In January 2006, the Internal Revenue Service (IRS) notified the County that CGH owed $14,393 in delinquent payroll taxes, penalties and interest for the periods ending June 30, 2004 and June 30, 2005. Section A.2.6 of the A-C Handbook requires the Agency to comply with all federal and State requirements for withholding payroll taxes, reporting, filing, and all applicable tax deposits.

In February 2006, DCFS indicated that CGH had paid part of the IRS liability, and a repayment plan had been established for the remaining balance. DCFS needs to ensure that foster care funds are not used to pay penalties and interest to the IRS since these costs are unallowable according to the Circular.

Recommendation

5. **DCFS ensure that foster care funds are not used to pay penalties and interest to the IRS.**

CONTRACT COMPLIANCE AND INTERNAL CONTROLS

We noted several contract compliance issues and internal control weaknesses. If DCFS contracts with CGH in the future, DCFS will need to ensure that CGH management takes action to address the internal control recommendations in this report. DCFS will also need to monitor to ensure the corrective actions result in permanent changes.

Unaudited Financial Statements

Section 11.8 of the Contract requires CGH to have an annual or triennial financial audit conducted by an independent auditor in accordance with generally accepted auditing standards. CGH has not had a financial audit completed since fiscal year 2000-01.

Recommendation

6. **If DCFS considers contracting with CGH in the future, DCFS ensure that CGH management submits audited financial statements at least once every three years.**

Disbursement Procedures

We noted the following weaknesses in the Agency's disbursement procedures:

- CGH did not have any documentation that the children were receiving the required monthly clothing allowance.

- CGH did not consistently write or stamp "Paid" on vendor invoices. None of the 30 invoices we reviewed were marked "Paid". In addition, the supporting documentation for 28 of the 30 expenditures was not referenced to the cancelled check. To prevent duplicate payments and to link supporting documents to the corresponding cancelled checks, all invoices should be marked "Paid" and referenced to cancelled checks.

- CGH deposited five of the 67 County warrants (7%) an average of 102 days after the warrant issue date. The A-C Handbook Section 1.2 states that cash receipts (i.e., cash, or checks) totaling $500 or more shall be deposited within one day of receipt.

- Two of 55 expenditures were not recorded in the Agency's general ledger.

Recommendations

If DCFS considers contracting with CGH in the future, CGH management:

7. **Maintain documentation that children are receiving a monthly clothing allowance.**

8. **Ensure all vendor invoices and receipts are marked "Paid" and referenced to check numbers.**

9. **Ensure cash receipts totaling $500 or more are deposited within one day of receipt.**

10. **Ensure all expenditures are property recorded in the Agency's general ledger.**

Payroll Controls

CDSS MPP Section 11-402 requires that supporting documentation be maintained for all program expenditures, including employee pay rates. We requested ten employee personnel files to review. CGH was unable to locate three (30%) of the files. Of the seven files provided, three did not contain the employee's authorized pay rate, or history. In addition, three employees' authorized pay rates did not agree to their actual pay. Despite the absence of pay rate in the employees' personnel file, we verified that

the pay rates were reasonable based on the applicable Child Welfare League of America Salary Study.

If DCFS considers contracting with CGH in the future, CGH management should ensure that employee pay rates are consistently documented and updated in the employee's personnel file to ensure that payroll expenditures are authorized and accurate.

Recommendation

11. **If DCFS considers contracting with CGH in the future, CGH management should ensure employee pay rates are consistently documented and updated in the employee's personnel file.**

Payable to the Executive Director

CGH's June 30, 2005 financial records indicated that the Agency owed the Executive Director $18,778. However, the Agency was unable to provide any documentation to substantiate the debt. Since the Agency was unable to substantiate the debt, the liability to the Executive Director should be removed from the financial statements.

Recommendation

12. **CGH remove the payable to the Executive Director from the Agency's financial records.**

Compliance with Insurance Requirements

According to the group home contract, CGH was required to maintain workers' compensation insurance. Failure to maintain the required insurance is a material breach of the contract. After our fieldwork, the State Compensation Insurance Fund notified us that CGH's workers' compensation insurance had been cancelled, reinstated and cancelled again.

Recommendation

13. **If DCFS considers contracting with CGH in the future, DCFS monitor to ensure that CGH maintains the required workers' compensation insurance.**

Bank Reconciliations

A-C Handbook Section 1.4 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. CGH's preparer does not sign and date the bank reconciliations and management does not review the reconciliations.

Recommendation

14. **If DCFS considers contracting with CGH in the future, CGH management ensure the Agency's bank reconciliations are signed and dated by both the preparer and the reviewer, and that the reconciliations are reviewed by management for appropriateness and accuracy.**