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August 1, 2007

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 UNITED CARE, INC. - A FOSTER FAMILY AGENCY AND GROUP HOME FOSTER CARE CONTRACTOR**

Attached is our report on United Care, Inc. (United or Agency) fiscal operations from January 1, 2005 through December 31, 2005. The Department of Children and Family Services (DCFS) contracted with United to serve as a Foster Family Agency (FFA) to recruit, certify, train and support foster family homes, and to provide treatment and support for DCFS children placed in the homes. United is located in the Second Supervisorial District.

From January 1, 2005 through December 31, 2005, United had 232 children placed in approximately 129 certified homes. DCFS paid United a monthly rate, for each child placement, established by the California Department of Social Services' (CDSS). CDSS requires FFAs to pay their foster parents at least 40% of the funds they receive. United received $3,954,796 in FFA funds from DCFS, and paid $1,698,266 (43%) of the funds directly to foster parents, which exceeds CDSS' minimum.

United was also licensed to operate three group homes (GHs), each with a resident capacity of six children. DCFS paid United $4,858 per child per month, based on a rate set by CDSS, for a total of $964,805 in foster care funds.

Scope

Our review was intended to determine whether United 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 the Agency's accounting records, internal controls and compliance with applicable federal, State and County guidelines for group home foster care funds.

Summary of Findings

We identified $274,608 in questioned costs and $1,795 in overpayments from DCFS. We noted that 87% of the expenditures on the Agency's American Express credit cards were either not supported with original receipts or were unallowable expenditures. In addition, we noted that United needs to strengthen its internal controls over accounting procedures, disbursements, personnel and payroll, and bank reconciliations. United also needs to comply with the County contract insurance requirements. Finally, we noted that United hired a Certified Public Accountant who did not meet the independence requirements to perform the Agency's annual financial audit for 2004 and 2005. Details of our findings are discussed in the attached report.

We have recommended that DCFS resolve the questioned costs and, to the extent possible, pursue the collection of the disallowed amounts. In addition, DCFS needs to ensure that United's management takes appropriate action to address the recommendations in this report, and that the actions taken result in permanent changes.

Review of Report

We discussed our report with United management on April 11, 2007. The Agency will provide their response to the 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 United's 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:MMO:JLS:MM:RHL:MD

Attachment

c: William T Fujioka, Chief Executive Officer
Department of Children and Family Services
Patricia S. Ploehn, Director
Susan Kerr, Chief Deputy Director
United Care Inc.
Craig Woods, Executive Director
Board of Directors
California Department of Social Services
Cora Dixon, Bureau Chief, Foster Care Audit Bureau
Sheliah Dupuy, Bureau Chief, Foster Care Rates Bureau
Public Information Office
Audit Committee
Commission for Children and Families

UNITED CARE INCORPORATED
FISCAL REVIEW

REVIEW OF EXPENDITURES/REVENUES

We identified $274,608 in questioned costs and $1,795 in overpayments. Details of these costs/revenues are discussed below.

Applicable Regulations and Guidelines

United is required to operate its FFA and GH's in accordance with the following federal, State and County regulations and guidelines:

- GH Contract, including Exhibit I, 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 $91,574 in unallowable expenses.

- $82,837 in credit card expenditures, consisting of $81,013 in personal expenditures made by two Agency cardholders, $1,606 in finance charges and late fees, and $218 in fundraising expenses. Personal expenditures are not allowable. In addition, Sections 16 and 23 of the Circular indicate that fines, penalties, and interest payments are also unallowable costs. Further, Section 17 of the Circular states that fundraising costs are unallowable.
- $4,837 in interest on an equity line of credit that was used to finance operations. Section 23a of the Circular states that interest on borrowed capital is unallowable. It should be noted that the principal owed on the equity line of credit was repaid in full subsequent to our review period.
- $3,164 in payments to a mental health program consultant and a fundraising consultant. The A-C Handbook states that only expenditures that are necessary, proper and reasonable to carry out the purposes and activities of the program are

allowable. FFA funds should not be used to pay mental health program costs. Section 17 of the Circular states that fund raising costs are unallowable.

- $636 in interest, penalties and fines, consisting of $231 in early withdrawal penalties for a savings account, $213 in insurance/lease payment late fees and postage refill finance charges, $157 in non-sufficient fund and returned check fees and a $35 parking violation. Sections 16 and 23 of the Circular indicate that fines, penalties, and interest payments are not allowable costs.

- $100 charitable donation to a dance company. 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. Section 12 of the Circular further states that contributions and donations are unallowable.

Unsupported/Inadequately Supported Costs

The A-C Handbook states that all revenues and expenditures shall be supported by original vouchers, invoices, receipts, timecards, travel logs, contract and loan agreements and/or other documentation, and that unsupported expenditures shall be disallowed upon audit.

We identified $183,034 in FFA and GH program expenditures that were either unsupported or inadequately supported.

- $131,087 in unsupported and inadequately supported credit card expenditures. Expenditures for $118,329 were charged to the Agency's American Express credit cards from 2003 to 2005. The remaining $12,758 expenditures were made on six other Agency credit cards during 2005. The Agency provided credit card statements and some internally generated purchase orders as support for these expenditures. However, without original invoices or receipts, we cannot verify that the expenditures benefited the FFA/GH programs. The credit card statements indicated that the expenditures were for office supplies, gasoline, food, hotel accommodations, cell phone charges, equipment rentals and other items. Section B.2.4 of the A-C Handbook requires that all credit card disbursements 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 alone are not sufficient documentation for credit card purchases.

- $33,460 in inadequately supported payroll expenditures. One employee worked on multiple programs but did not allocate his time among the programs for a total of $32,500 in payroll expenditures. We noted that the employee spent a least part of his time working on an unrelated Mental Health program. The remaining $960 in unallowable costs was related to an employee who did not have a timecard/time report or a personnel file. The A-C Handbook states that timecards or time reports must indicate total hours worked each day by program and total hours charged to each of the contractor's programs.

- $11,672 in unsupported and inadequately supported payments for various items, such as a banner, carpet stretching, vehicle repairs, office furniture, office equipment, training, membership fees, theme park, hotels, and employee reimbursements for gift cards and restaurant expenses.

- $4,006 in inadequately supported payments to two independent contractors for accounting consulting services and legal services. In one instance, the Agency did not have a written contract with the vendor, and in the other instance, there was a written contract, but there was no invoice to support the disbursement.

- $2,809 in payments for gasoline, carwash coupons and insurance for the FFA vehicle. While this vehicle was undoubtedly used for FFA business, United did not maintain mileage records or other documentation for the FFA vehicle to show what portion of the usage was related to the program. A-C Handbook Section A.3.2 requires agencies to maintain vehicle mileage logs showing the dates, destination and headquarters, purpose of trip and mileage.

Overpayments by DCFS

We reviewed the payment records for nineteen FFA and GH children and noted three unresolved overpayments from DCFS, totaling $1,795. DCFS sent the Agency an invoice for each overpayment, with the most recent invoice sent in April 2006. The contract stipulates that the Contractor and County shall attempt to resolve payment discrepancies within thirty days of the invoice.

Recommendations

DCFS management:

1. **Resolve the $274,608 in unallowable and unsupported/inadequately supported costs and pursue the collection of any disallowed amounts.**

2. **Work with United management to resolve the $1,795 in overpayments and monitor to ensure that over/underpayments are resolved timely.**

United management:

3. **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 and FFA.**

4. **Consistently maintain adequate supporting documentation for all foster care expenditures, including original itemized receipts/invoices and mileage logs. In addition, ensure timecards or time reports are prepared by all employees for each pay period that indicate total hours worked by program.**

CONTRACT COMPLIANCE AND INTERNAL CONTROLS

We noted several contract compliance issues and internal control weaknesses. DCFS should ensure that United management takes action to address each of the issues discussed in this report and monitor to ensure that the actions result in permanent changes.

Insurance Coverage

The FFA and GH contracts require United to have automobile liability insurance with a limit of no less than $1 million per incident, for all owned, hired (i.e., leased or rented) and non-owned vehicles, or coverage for any auto. The contract also requires that the County be given written notice by mail at least thirty days in advance of cancellation for all polices.

We noted that, in three of the Agency's four vehicle insurance policies, the Group Home Administrator was the only authorized driver. When other agency staff drive those vehicles, they are not insured, which exposes the Agency and the County to substantial liability.

We also noted that the policies do not cover rented/leased and non-owned vehicles as required. In addition, the vehicle insurance and Workers' Compensation policies only provide a ten-day cancellation notice, instead of the required 30-day notice.

Recommendation

5. **United management ensure that the Agency's insurance policies comply with the contract requirements.**

Accounting Procedures

We reviewed 149 expenditures, and noted the following weaknesses in the Agency's accounting procedures:

- 36 transactions (24%) were inconsistently classified in the accounting records. For example, payments made for a line of credit were recorded as interest expense, unknown expense, and/or credit line during the year. The A-C Handbook states that the contractor must consistently post transactions that are of a similar nature to the same account.

- 23 transactions (15%), totaling $7,691, were not recorded in the Agency's accounting records. These payments were made by electronic fund transfer directly from the Agency's bank account. As a result, the Agency's expenditures were understated by that amount. The Agency should ensure it records all expenditures in the accounting records.

- 15 transactions (10%), totaling $4,094, were charged to the wrong program (i.e., FFA expenses were charged to the GH program, and vice versa). Agency management was unable to explain why these transactions were charged to the wrong programs. United needs to ensure all expenditures are consistently charged to the appropriate program.

- 11 expenditures (7%) were recorded in the Agency's accounting records. However, it was unclear to which program the expenditure had been charged. United management was unaware of this problem but subsequently advised us that it was due to their accounting software. United indicated that they would consult with the software vendor to resolve this problem.

- United does not reconcile payments received from the County by direct deposit to the list of payments from the County. This reconciliation is necessary to ensure all payments from the County are received and accounted for and to identify possible over/under payments.

- United overstated its expenditures by $9,536 when recording foster parents' liability insurance payments. United withheld $16,210 from its payments to foster parents to pay for foster parents' liability insurance. While United recorded the foster parent payment and withholding as an expense, it did not separately account for the funds withheld as a liability in the Agency's books. As a result, the payment for the foster parent insurance was recorded as United's own insurance expense, which overstates United's expenditures.

- United does not maintain a fixed asset listing. A-C Handbook Section 4.2 requires that agencies maintain a current listing of fixed assets, including the item description, serial number, date of purchase, acquisition cost and sources of funding.

- United incurred $6,130 in bank service fees for one of their checking accounts. The fees resulted from enrolling in a checking analysis account that grants credits when the Agency maintains an average balance of $120,000 a month on the checking account, which are offset by bank service fees based on the amount of services used for the month. The Agency consistently incurred more bank service fees than credits. The Agency should explore alternative banking services to limit monthly service fees.

Recommendations

United management:

6. **Ensure all transactions are consistently classified and recorded in the accounting system.**

7. **Ensure transactions are consistently charged to the appropriate program.**

8. **Resolve problems with their accounting software to ensure that transactions are consistently and correctly recorded.**

9. **Ensure it reconciles the payments received to the list of County payments to verify that all payments are received.**

10. **Ensure it properly accounts for foster parent payments and foster parent liability deductions.**

11. **Maintain a fixed asset listing in compliance with the A-C Handbook.**

12. **Explore alternative banking services to reduce the monthly service fees.**

Disbursement Procedures

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

- United does not consistently mark invoices "Paid" or reference invoices to the cancelled checks. Eighty-seven of 149 invoices (58%) were not marked "Paid" or referenced to a check, and 30 (20%) were marked "Paid" but were not referenced to a check. To prevent duplicate payments and to link supporting documents to the corresponding cancelled checks, all invoices should be marked "Paid" and referenced to the cancelled checks.

- The Agency does not require a second signature on checks. We noted the Executive Director approved three reimbursements to himself for a total of $1,262. The A-C Handbook states that a second signature is required on all checks, unless otherwise specified in the contract.

Recommendations

United management:

13. **Ensure all vendor invoices and receipts are consistently marked "Paid" and referenced to the cancelled checks.**

14. **Require a second signature on all checks, as required by the A-C Handbook.**

Personnel and Payroll Records

We noted the following weaknesses in the Agency's personnel and payroll procedures:

- 6 of 13 personnel files (46%) reviewed did not contain the current salary rate for the employee. CDSS MPP Section 11-402 requires that supporting documentation be maintained, including salary rates. United needs to ensure that employee pay rates are consistently documented in the personnel files.

- The Agency does not maintain a benefits log to monitor employees' accrual and use of vacation and sick time. 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 when hours are used.

- A $4,300 salary overpayment to one employee for July 16, 2005 through July 31, 2005 had not been collected by the Agency as of the end of our review. United indicated they were aware of the overpayment but could not explain why they had not collected from the employee. The Agency needs to ensure it resolves the overpayment as soon as possible.

- Two requests for payment of accrued vacation time were processed without the supervisor's approval.

Recommendations

United management:

15. **Ensure personnel files contain current authorized salary amounts or hourly rates of pay.**

16. **Maintain a benefits log to monitor the use and accrual of vacation and sick time.**

17. **Resolve salary overpayments timely.**

18. **Ensure requests to payments for accrued vacation are properly approved.**

Financial Audit

The California State Department of Social Services (CDSS) requires FFA and GH providers to submit a Financial Audit Report. WIC Section 11466.21(a)(4) requires that the audit be conducted by a Certified Public Accountant (CPA) who has no direct or indirect relationship with the functions or activities being audited, or with the provider, its board of directors, officers or staff.

We noted that the CPA engaged to complete United's Financial Audit Reports for 2004 and 2005 is related to the accountant who kept the Agency's financial records during the audit periods. This relationship (uncle-niece) results in a lack of independence on the part of the CPA.

United management should notify CDSS that its 2004 and 2005 Financial Audit Reports were not prepared in accordance to WIC Section 11466.21(a)(4) .

Recommendation

19. United management notify CDSS that its 2004 and 2005 Financial Audit Reports were not prepared in accordance to WIC Section 11466.21(a)(4).

Reconciliations

In a September 9, 2005 report, Velazquez and Associates (Velazquez), the United's interim accounting firm, noted that the accountant previously employed by the Agency used an automatic reconciling feature in the accounting software, which resulted in incorrect adjusting entries in the accounting records and created a balance in the "Opening Balance Equity Account". Velazquez recommended that the Agency conduct an analysis of the Opening Balance Equity Account and determine how to bring the balance in this account to zero. As of August 2006, United had not implemented Velazquez' recommendation and the Opening Balance Equity account had a balance of ($9,548).

We also noted that United's bank reconciliations were not completed within 30 days of the bank statement date, were not reviewed by management, and were not signed and dated by the preparer and reviewer as required by the A-C Handbook. United needs to ensure that bank reconciliations are completed within 30 days of the bank statement date, reviewed by management, and signed and dated by both preparer and reviewer.

Recommendations

United management:

20. Implement Velazquez' recommendation to conduct an analysis of the Opening Balance Equity Account and determine how to bring the balance in this account to zero.

21. Ensure the Agency's bank account reconciliations are completed within 30 days of the bank statement date, are reviewed by management and signed by both preparer and reviewer.