COUNTY OF LOS ANGELES
DEPARTMENT OF AUDITOR-CONTROLLER

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WENDY L. WATANABE
ACTING AUDITOR-CONTROLLER

ASST. AUDITOR-CONTROLLERS

ROBERT A. DAVIS
JOHN NAIMO
MARIA M. OMS

September 18, 2008

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

FROM: Wendy L. Watanabe
Acting Auditor-Controller

SUBJECT: **FISCAL REVIEW OF HUDSON LYNDSEY FOSTER FAMILY AGENCY (aka PSYCH MED, INCORPORATED) – A FOSTER CARE CONTRACTOR**

Attached is our report on the fiscal operations of Hudson Lyndsey Foster Family Agency (Hudson FFA or Agency), also known as Psych Med, Incorporated, from January 1, through December 31, 2006. The Department of Children and Family Services (DCFS) contracts with Hudson FFA to serve as a Foster Family Agency (FFA) to recruit, certify, train and support foster family homes. The Agency's administrative office is located in Anaheim.

Hudson FFA had 95 children placed by Los Angeles County in 20 certified foster homes during 2006. DCFS paid Hudson FFA between $1,589 and $1,865 per month for each foster child, for a total of $670,261. Hudson FFA paid $265,466 (40%) directly to the foster parents, which meets the State's minimum requirement.

Scope

The purpose of the review was to determine whether Hudson FFA complied with the contract terms and appropriately accounted for and spent foster care funds on allowable and reasonable expenditures. We also evaluated Hudson's expenditure and revenue documentation, internal controls and compliance with federal, State and County fiscal guidelines governing FFA foster care funds.

Summary of Findings

We identified a total of $80,189 in unallowable costs and $29,030 in unsupported/inadequately supported costs. In addition, DCFS and the Agency need to work together to resolve potential overpayments.

We noted that the Hudson FFA's Certified Public Accountant's opinion on the Agency's audited financial statements for the years ended December 31, 2003, 2004 and 2005 included a going concern qualification, as a result of operating losses and negative net assets in each of the three years. The qualification indicates there are financial issues which may affect the Agency's ability to continue operations. Hudson's internally generated financial statements indicate that the Agency incurred an additional operating loss of $132,694 for 2006.

Hudson FFA also owes $35,453 in delinquent federal payroll taxes, interest and penalties, and is in the process of resolving $156,198 in delinquent State taxes, interest and penalties, which the Agency is disputing.

Finally, the Agency needs to resolve several deficiencies in its internal controls over the disbursement of foster care funds that contributed to the questioned expenditures discussed above. We also noted that Hudson FFA needs to strengthen its controls over accounting and disbursements, loan agreements, timely depositing of funds, bank reconciliations, automobile insurance coverage, and accurately reporting independent contractors' payments on federal tax Form 1099. Details of our findings are discussed in the attached report.

The findings noted in this report are significant and Hudson's corrective action plan needs to address the recommendations in this report and describe how they will:

- Provide an adequate quality level of care while addressing their continuing operating losses.

- Pay the federal and any State tax liability without using current period foster care funds.

Further, we have recommended that DCFS resolve the questioned costs and collect any overpayments and disallowed amounts. If the Agency is unable to provide an acceptable corrective action plan and correct these deficiencies promptly, DCFS should consider terminating its contract with Hudson FFA.

Review of Report

We discussed our report with Hudson FFA's management on March 6, 2008. The Agency's response, which is incorporated into DCFS' Fiscal Corrective Action Plan (attached), indicates the Agency's general agreement with our findings and

recommendations. However, the Agency did take exception to our disallowing their use of current period foster care funds to pay for prior year taxes (2003-2005) and fundraising. As stated in the Corrective Action Plan, DCFS agrees with the audit findings and is requiring the Agency to repay the questioned amounts. In the Corrective Action Plan, the Agency also outlined several areas where they plan to reduce costs without adversely affecting the quality of care provided to foster children.

We thank Hudson's management and staff for their cooperation during our review. Please call me if you have any questions, or your staff may contact Jim Schneiderman at (626) 293-1101.

WLW:MMO:JLS:MM

Attachments

c: William T Fujioka, Chief Executive Officer
Patricia S. Ploehn, Director, Department of Children and Family Services
Susan Kerr, Senior Deputy Director, Department of Children and Family Services
Cynthia Powell, Executive Director, Hudson Lyndsey Foster Family Agency
Board of Directors, Hudson Lyndsey Foster Family Agency
Cora Dixon, Bureau Chief, Foster Care Audits Bureau, California Department of Social Services
Public Information Office
Audit Committee Members
Commission for Children and Families

Hudson Lyndsey Foster Family Agency (aka Psych Med, Inc.)
Fiscal Review

REVIEW OF EXPENDITURES/REVENUES

We identified $80,189 in unallowable costs and $29,030 in unsupported/inadequately supported costs. In addition, DCFS and the Agency need to work together to resolve potential overpayments. Details of these expenditures/overpayments are discussed below.

Applicable Regulations and Guidelines

Hudson FFA 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 the 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).

Unallowable Expenditures

The Agency incurred $80,189 in unallowable expenditures:

- $73,939 in delinquent payroll taxes, interest and penalties for September 30, 2004 through September 30, 2005, and penalties assessed for untimely filing of the federal 2003 Organization Exempt from Income Tax Return (Form 990).
- $6,250 in other unallowable costs; consisting of $909 in non-sufficient fund (NSF) and overdraft fees, $2,341 in interest charges and late fees, and $3,000 paid to a contractor for fundraising activities, where the contractor's invoices identified fundraising as part of the billed services.

Circular Sections 16 and 23 state that penalties and interest are unallowable. In addition, Circular Section 17 states that fundraising expenses incurred to raise capital or obtain contributions are unallowable. Finally, A-C Handbook Section A.2.6 states that the Agency will ensure compliance with all applicable federal and State

requirements for withholding payroll taxes, reporting, filing and all applicable tax deposits. The Agency has not complied with federal tax requirements. Using current period foster care funds to pay for prior years' delinquent taxes is an unallowable use of County foster care funds.

Unsupported/Inadequately Supported Expenditures

The Agency incurred $29,030 in expenditures that were either unsupported, or were inadequately supported.

- $24,667 in inadequately supported credit card payments. The Agency provided cancelled checks issued to credit card companies, but no credit card statements, itemized receipts or invoices showing the specific items purchased.

- $3,980 in inadequately supported withdrawals from the Agency's bank accounts, for which no itemized receipts, invoices or other supporting documentation were provided for our review.

- $383 in inadequately supported expenditure involving a payment to Staples. The Agency did not provide any receipts, invoices or billing statements from Staples for 2006. Therefore, we were unable to determine if this expense was for the FFA program, or if this payment involved any unallowable finance charges or late fees.

A-C Handbook Section A.3.2 states that all expenditures must be supported by original invoices, receipts, cancelled checks or other documentation, and that unsupported expenditures will be disallowed upon audit. A-C Handbook Section B.2.4 also states that credit card disbursements must be supported by original invoices, store receipts or other external documents indicating the items purchased and the employee making the purchases.

Recommendations

1. **DCFS management resolve the $109,219 ($80,189 + $29,030) in questioned costs and collect any disallowed amounts.**

Hudson FFA management:

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

3. **Ensure that foster care funds are used for allowable expenditures to carry out the purpose and activities of the Agency.**

FINANCIAL VIABILITY

The Agency's 2003 through 2005 audited financial statements indicated that the Agency was operating at a loss and had negative net assets, which raise substantial doubt about Hudson FFA's ability to continue as a going concern. Hudson FFA's unaudited 2006 financial statements also show a net loss of $132,694. In addition, the Agency has a substantial liability to the federal government, and may have a liability to the State for delinquent payroll taxes, and related penalties and interest.

Hudson FFA management needs to develop a plan describing how it will continue to provide an adequate level of care while addressing its ongoing operating losses. Given the Agency's tenuous financial position, DCFS must carefully monitor Hudson FFA to ensure that service quality is maintained at an acceptable level.

Recommendations

4. **Hudson FFA management develop a plan demonstrating how it will provide an adequate level of care while addressing its ongoing operating losses.**

5. **DCFS management carefully monitor Hudson FFA to ensure that service quality is maintained at an acceptable level.**

PAYROLL TAX LIABILITIES

The Agency owes $35,453 in delinquent federal payroll taxes, penalties and interest for the tax periods ending December 2005, March 2006 and June 2006.

In addition to the federal taxes, Hudson FFA's 2005 audited financial statements identify $156,198 in potential unpaid State payroll taxes, penalties and interest resulting from the Agency's classification of social workers as independent contractors, instead of as employees. This matter is currently under appeal.

These liabilities are not recorded on the Agency's financial records, but were classified as Commitments and Contingencies in a footnote to the 2005 financial statements. The Agency subsequently began repaying the federal tax liability and was developing a repayment plan which indicates the Agency acknowledged that it has a liability for these taxes. The federal tax liability and any delinquent State taxes for which the Agency is ultimately found liable should be recorded in Hudson FFA's financial records as liabilities.

Further, Hudson FFA cannot use current period foster care funds to pay prior years' taxes, penalties and interest. As part of Hudson FFA's plan to DCFS, the Agency needs to indicate how they will repay the prior years' taxes without using current period foster care funds. The Agency should also keep DCFS informed on the status of its

appeal of the State payroll tax issue until it is resolved, due to the significant impact this issue may have on the Agency's financial condition.

Recommendations

6. **DCFS management ensure that current period foster care funds are not used to pay prior years' taxes or any penalties and interest.**

Hudson FFA management:

7. **Address in their plan to DCFS how they will repay their prior years' tax liabilities without using current period foster care funds.**

8. **Record the liability for federal payroll taxes, interest and penalties, and any delinquent State taxes for which the Agency is ultimately found liable, in the Agency's financial statements.**

9. **Keep DCFS informed of the status of the State payroll tax issue until resolved.**

POTENTIAL DCFS OVERPAYMENTS

DCFS records show some overpayments made to the Agency. DCFS and the Agency should work together to resolve the overpayments and DCFS should collect any verified overpayments. Hudson management should ensure that any future payment discrepancies are immediately reported to DCFS and any overpaid amounts are repaid promptly.

Recommendations

10. **DCFS management work with Hudson to resolve the overpayments and DCFS should collect any verified overpayments.**

11. **Hudson's management ensure that any future payment discrepancies are immediately reported to DCFS and any overpaid amounts are repaid promptly.**

CONTRACT COMPLIANCE AND INTERNAL CONTROLS

We noted several contract compliance issues and internal control weaknesses. DCFS should ensure that Hudson FFA's management takes action to address each of the recommendations in this report. DCFS should also monitor to ensure the actions result in permanent changes.

Accounting and Disbursements

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

- Twelve checks, totaling $5,563, in which the payee and check signer were the same employee. Most of these checks were for petty cash. On checks were the signer is also the payee, a second signature by someone independent (such as a Board member) should be required to verify the appropriateness of the expense.

- Five checks, totaling $8,527, were made payable to Cash. A-C Handbook Section B.2.1 states that checks should not be payable to Cash.

Recommendations

Hudson FFA management:

12. **Require a second signature by an independent party on all checks where the payee and the check signer are the same employee.**

13. **Ensure that checks are not made payable to Cash.**

Loan Agreements

The Agency received loans from three sources, the Executive Director, the Assistant Administrator and the Shelby Renee Educational Center. As of December 31, 2006, the Agency's unaudited financial statements identified $54,567 in loans payable. However, the Agency did not have written agreements for some loans made by these sources. A-C Handbook Section A.3.2 states that loans to the Agency by individuals should be supported by a written agreement.

Recommendation

14. **Hudson FFA management establish written agreements for all loans indicating the amounts borrowed and the repayment terms.**

Untimely Deposits

During our review period, 175 Los Angeles County warrants, totaling $145,755, were deposited into the Agency's bank account more than ten days after the issue date. Five of these warrants were deposited as long as 61 days from the issue date. A-C Handbook Section B.1.2 states that cash receipts 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 occurs first.

To ensure that receipts are not lost or stolen, and improve cash flow, the Agency should ensure that County warrants are deposited timely, and consider having County payments electronically deposited directly into the Agency's bank account.

Recommendation

15. Hudson FFA management ensure that Los Angeles County warrants are deposited timely, and consider having its County payments electronically deposited directly into the Agency's bank account.

Bank Reconciliations

A-C Handbook Section B.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. Reconciling items should be resolved timely.

For the general operating account, we noted the following:

- Bank reconciliations for the months of April and October 2006 were not provided for our review.
- Seven of the ten monthly bank reconciliations available for review were not prepared within 30 days of the bank statement date.
- None of the ten monthly bank reconciliations reviewed were signed and dated by the preparer.
- Twenty five checks totaling $16,036 were outstanding for more than 6 months.

For the payroll account, we noted the following:

- Bank reconciliations for the months of August, September, October, November and December 2006 were not provided for our review.
- Four of the seven monthly bank reconciliations reviewed were not prepared within 30 days of the bank statement date.
- None of the seven monthly bank reconciliations reviewed were signed and dated by the preparer.
- Fifty checks totaling $24,215 were outstanding for more than 6 months.

Recommendations

Hudson FFA Management:

16. **Ensure the Agency prepares monthly bank statement reconciliations within 30 days of the bank statement date, and that the reconciliations are signed and dated by the preparer.**

17. **Review and cancel any checks that are outstanding for six months and reissue, if appropriate.**

Automobile Insurance

The Agency does not have insurance coverage for its owned automobiles. According to the Foster Care Contract, Hudson FFA is required to maintain automobile insurance. Failure to maintain the required insurance is a material breach of the Agency's Contract with the County, and makes the Agency vulnerable if it is found liable for accidents involving agency vehicles.

Recommendation

18. **Hudson FFA management maintain the insurance coverage required by the Contract.**

Independent Contractors

A-C Handbook Section A.2.6 states that the Agency will comply with all applicable federal and State requirements for reporting and filing independent contract income on 1099s. Two independent contractors' payments on their 1099s did not agree with the Agency's general ledger. Specifically, one contractor's total on the general ledger was $195 less than reported on the 1099. For the other contractor, the amount on the general ledger was $360 more than reported on the 1099.

Recommendation

19. **Hudson FFA management ensure that payments made to independent contractors are accurately reported on the 1099 Forms.**

County of Los Angeles
DEPARTMENT OF CHILDREN AND FAMILY SERVICES
425 Shatto Place, Los Angeles, California 90020
(213) 351-5602

PATRICIA S. PLOEHN, LCSW
Director

Board of Supervisors
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First District
YVONNE B. BURKE
Second District
ZEV YAROSLAVSKY
Third District
DON KNABE
Fourth District
MICHAEL D. ANTONOVICH
Fifth District

June 27, 2008

Cynthia Powell, Executive Director
Hudson Lyndsey Foster Family Agency
5241 Santa Ana Canyon Road, Suite 160
Anaheim, CA 92807

Dear Ms. Powell:

AUDITOR-CONTROLLER'S FISCAL AUDIT REPORT ON HUDSON LYNDSEY FOSTER FAMILY AGENCY – A FOSTER FAMILY AGENCY CONTRACTOR

I have completed my review of the bank statements for February 2006, April 2006, July 2003, and August 2006 you submitted to me on June 18, 2008 and June 23, 2008. Your agency's stated intention for submitting these documents was to support your claim that the monies given to the agency by you were gifted monies. The copy of two check deposited on February 7, 2006 was included in your documentation. At the top of the copy of the checks someone has written "Loan" with an arrow pointing to the $5,000 check.

In the first paragraph of the first page of Attachment I of the Request for a Fiscal Corrective Action Plan mailed to you on June 3, 2008, the following statement appears: "**Note:** DCFS will only review documentation not previously provided to the Auditor-Controller". I have confirmed with Auditor-Controller staff that they did review the bank statements for the calendar year 2006.

After careful consideration, DCFS stands behind the Auditor-Controller's findings and expects Hudson-Lyndsey to enter into a repayment agreement to repay the $109,219 in questioned costs identified by the Auditor-Controller. The maximum time allowed to repay audit findings is five (5) years. I have attached a repayment schedule for your review.

Please call me at 213-351-3208 by July 7, 2008 to schedule an appointment to sign the repayment agreement.

Sincerely,

Sue Harper

Sue Harper, ASM III
Fiscal Monitoring and Special Payments

Enclosures
C: Russ Lingo, Auditor-Controller

County of Los Angeles
DEPARTMENT OF CHILDREN AND FAMILY SERVICES
425 Shatto Place, Los Angeles, California 90020
(213) 351-5602

PATRICIA S. PLOEHN, LCSW
Director

Board of Supervisors
GLORIA MOLINA
First District
YVONNE B. BURKE
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Third District
DON KNABE
Fourth District
MICHAEL D. ANTONOVICH
Fifth District

June 3, 2008

Cynthia Powell, Executive Director
Hudson Lyndsey Foster Family Agency
5241 Santa Ana Canyon Road, Suite 160
Anaheim, CA 92807

Dear Ms. Powell:

AUDITOR-CONTROLLER'S FISCAL AUDIT REPORT ON HUDSON LYNDSEY FOSTER FAMILY AGENCY - A FOSTER FAMILY AGENCY CONTRACTOR

We have reviewed your fiscal corrective action plan (FCAP) addendum with the submission dates of April 4 and 7, 2008 in response to the Auditor-Controller's draft fiscal audit report dated March 6, 2008. The FCAP fully addresses thirteen recommendations; however it does not appropriately address six of the recommendations (See Attachment I).

With regard to the $80,189 in unallowable expenditures, in accordance with OBM Circular A-122 and the Los Angeles County Auditor-Controller's Handbook, DCFS is unable to allow any of these costs. Your agency did not provide supporting documentation for the $29,030 in unsupported expenditures, therefore, a total of $109,219 must be repaid to the Department (See Attachment II). Your agency may not use current year foster care funds to repay these funds. Please call me at 213-351-3208 to schedule an appointment to sign a repayment plan. I have enclosed a five-year repayment plan for your review (See Attachment III). The signed repayment plan must be in place by June 15, 2008. Having a signed repayment plan in place will resolve Recommendations # 1, 6, and 7).

Recommendations 9, 10, and 11 require your ager
providing information to DCFS to resolve overpayment is
information may result in DCFS taking adverse actio
correspondence regarding this audit must be submitted t

Sue Harper, ASM III
Fiscal Monitoring & Special Paymen
425 Shatto Place, Room 304
Los Angeles, CA 90020

Sincerely,

Sue Harper, ASM III
Fiscal Monitoring and Special Payments

7005 0390 0003 2907 3239

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Cynthia Powell, Executive Director
Hudson Lyndsey Foster Family Agency
5241 Santa Ana Canyon Rd., Suite 160
Anaheim, California 92807

PS Form 3800, June 2002 See Reverse for Instructio

ATTACHMENT I

FISCAL REVIEW OF
HUDSON LYNDSEY FOSTER FAMILY AGENCY
A FOSTER FAMILY AGENCY CONTRACTOR

Note: DCFS will only review documentation not previously provided to the Auditor-Controller.

Summary of Recommendations

Based on the FCAP materials dated April 4, 2008 and April 7, 2008, submitted by Hudson's, the status of each recommendation is summarized as follows:

- 13 Recommendations (2, 3, 4, 5, 8, 12, 13, 14, 15, 16, 17, 18, and 19) were fully addressed.
- 6 Recommendations (1, 6, 7, 9, 10, and 11) were partially addressed.
- 4 Recommendations (1, 5, 6, and 10) directed to the Department.

Auditor-Controller Recommendations

1. **DCFS management resolve the $109,219 in questioned costs and, if appropriate, collect any disallowed amounts.**

   Hudson's Proposed FCAP: Remaining items to address with supporting documentation or explanation:

   Delinquent Payroll Tax @ $73,939

   The first item to address is the disagreement of interpretation to the statement that Section A.2.6 of the A-C Handbook states that using current period foster care funds to pay for prior years delinquent taxes is an unallowable use of County foster care funds.

   We agree that interest and penalties are unallowable expenses per the A-C Handbook, however, do not find or agree with not having the ability to use foster care funds for the purpose of **actual payroll tax.**

   As the foster care program rates are fixed by the State of California, and this is not a reimbursement program, we cannot agree to the support of the statement. Had our 2004/2005 accountant properly accrued expenses for the appropriate years, this would not be an issue as accruals are acceptable.

   Following is a break down of the actual unallowable statutory fines for the quarters referrenced in audit:

09/2004	1,492.99	
12/2004	1,978.03	
03/2005	1,969.88	
06/2005	1,017.49	
09/2005	1,510.60	
	7,968.99	**Total unallowable interest/penalties**

Additionally, an amount of $27,779 was paid for failure to file penalties, tax form 990/2003.

Hudson Lyndsey has used the same tax accounting service, Felix and Associates, for over 7 years. Our accounting firm maintained they filed this return timely and have given evidence for support. We expect full abatement of these monies with further proper allocation and re-assessment of other fines and penalties incurred because of this.

Since results have not been as timely as expected from our accounting service, Hudson Lyndsey has recently retained the services of an independent consultant/accountant to deal directly with these entities in resolution. We will continually update as to our progress and ultimate resolution.

Of the $73,939 that is stated in the final audit, we feel the only unallowable portion is $7,969.

Our attached audited financial statements: NOTE 1 – CONTINGENCIES state **"an officer of the Company made contributions to Psych Med totaling $45,976 representing mostly loans advanced to the Company which will not be repaid."**

This amount more that covers the unallowable interest and penalties incurred.

Hudson Lyndsey is contesting the unallowable expense of $3,000 paid to a contractor for 'fundraising activities'. We submitted additional documentation at the exit conference and are now copying your as you requested.

As a note to this response, there was no fundraising activity performed by this subcontractor. Hudson Lyndsey accepted a general billing with a standard reiteration of performance requirements on behalf of the subcontractor.

DCFS Response: Federal OMB Circular No. A-122 A. 2. states in part:

2. "Factors affecting allowability of costs. To be allowable under an award, costs must meet the following general criteria:

    c. Be consistent with policies and procedures that apply uniformly to both federally-financed and other activities of the organization.
    d. Be accorded consistent treatment.
    e. Be determined in accordance with generally accepted accounting principles (GAAP).
    f. Be adequately documented."

In addition, OMB Circular No. A-122 47.a states, "...taxes which the organization is required to pay and which are paid or accrued in accordance with GAAP...are allowable...".

As you can see from the above, A.2.e. **allowable** expenses must be determined **in accordance with generally accepted accounting principles (GAAP).** I disagree with your interpretation that an organization may pay prior year taxes with the current year's revenue. Taxes are to be paid on time, thus avoiding late fees, unallowable penalties and interest.

In addition, Section A.2.6 of the A-C Handbook states that a CONTRACTOR (or agency) <u>will ensure compliance</u> with all applicable <u>federal and State requirements for withholding payroll taxes, reporting, filing (941, DE-7, W-2, W-4 and 1099s), and all applicable tax deposits</u>. The fact that Hudson FFA did not ensure compliance is a violation of contract requirements and federal and State tax laws.

Using current period funds to pay for prior years' payroll taxes can compromise the care and services to the current foster children. It would be unacceptable for an agency to pay for all the current year's expenses and also pay for prior years' outstanding payroll taxes without any unrestricted net assets at year end. Hudson FFA does not have any unrestricted net assets or surplus of funds at year end.

The issues your agency has with your former accountant are outside of my purview and must be resolved by the agency. You state that "you expect full abatement of these monies". At such time as you reach resolution and receive a full abatement of these monies, I can meet with you to prepare an addendum to this report.

As to the monies paid to a contractor for 'fundraising activities', without proper documentation (an itemized invoice from the contractor) I cannot allow the $3,000 expenditure as fundraising is not allowable under OMB A-122.

In regard to your audited financial statement NOTE 1 – CONTINGENCIES stating: **"an officer of the Company made contributions to Psych Med totaling $45,976 representing mostly loans advanced to the Company which will not be repaid."** Were these monies considered "contributions" or "loans"? I was not provided any loan documents or donation receipts supporting this claim. While this amount would cover the unallowable interest and penalties incurred, the Auditor did not find the necessary documentation to link these costs with the "contributions" or "loans" made by an officer of the Company.

Therefore, DCFS disallows the entire $109, 219 and must be repaid.

2. **Hudson's management maintain adequate supporting documentation for all Agency expenditures, including original itemized receipts and invoices.**

Hudson's Proposed FCAP: The following is Hudson Lyndsey's Board-approved policy and procedure to ensure compliance pertaining to agency expenditures, including original itemized receipts and invoices.

All Hudson Lyndsey expenditures will have adequate supporting documentation prior to being submitted for approval. All requests for reimbursement or payment will be accompanied by original receipts. Copies of receipts will be maintained for an individual's records.

Statements of any kind, regardless of the expense, are not adequate unless properly supported.

Policy and Procedure Manual is in complete compliance with the A-C Handbook, OMB Circular 122 and the CDSS-MPP.

DCFS Response: DCFS accepts the agency policy.

3. **Hudson's management ensure that foster care funds are used for allowable expenditures to carry out the purpose and activities of the Agency.**

Hudson's Proposed FCAP: The following is Hudson Lyndsey's Board-approved policy and procedure to ensure that foster care funds are used for allowable expenditures to carry out the purpose and activities of the Agency.

Per OMB Circular A-122, General Principles/Costs, foster care funds are only allowable to carry out the purpose and activities of the Agency.

No individual will incur, nor approve any unusual expenditure without prior Management/Board approval.

DCFS Response: DCFS accepts the agency policy.

4. **Hudson's management, in consultation with its accountant, develop a plan demonstrating how it will provide an adequate quality level of care while addressing its ongoing operating losses.**

Hudson's Proposed FCAP: Hudson Lyndsey has developed a balanced budget. We recognize areas for monetary reorganization and made the changes with no adverse effect on our quality of care. Adherence to this budget has evidenced itself in our attached 2006 Statement of Activities.

Per our exit meeting response the following areas were addressed:

Office Staffing
The skill level of Hudson Lyndsey's employees has enabled us to reduce staff.

Vehicle Expense
The disposal of company vehicles has reduced the company overhead.

Building Rent/Lease
In 2006 we downsized our L.A. office from two spaces to one. Additionally, once our L.A. office lease expired in 2007 we moved offices with a monthly lease reduction of $5,500. The new office suite includes utilities and janitorial services.

Medical Insurance
As of 2007, Hudson Lyndsey has been secured a new medical package, the cost savings is approximately 60%.

DCFS Response: DCFS accepts the agency changes.

5. **DCFS management carefully monitor Hudson FFA to ensure that service quality is maintained at an acceptable level.**

Hudson's Proposed FCAP: Hudson Lyndsey Administrator and Supervising Social Worker meet on a bi-monthly basis for a Status Meeting, in regards to each Social Worker, their case loads and to audit the clients' charts to ensure all required documentation is completed and accurately filed. Upon request, all reports and/or documentation will be made available for DCFS Monitor in a timely manner.

DCFS Response: DCFS Fiscal staff accepts the agency policy. Program Monitoring staff will be made aware of the need for service quality monitoring.

6. **DCFS management ensure that foster care funds are not used to pay prior years' taxes or any penalties and interest.**

   Hudson's Proposed FCAP: Please note our response to Recommendation #1.

   NOTE 1 – CONTINGENCIES "an officer of the Company made contributions to Psych Med totaling $45,976 representing loans advanced to the Company which will not be repaid.

   This figure more than covers any unallowable fines, penalties, and interest paid with other than current year foster care funds.

   DCFS Response: In regard to your audited financial statement NOTE 1 – CONTINGENCIES stating: **"an officer of the Company made <u>contributions</u> to Psych Med totaling $45,976 representing mostly <u>loans</u> advanced to the Company which will not be repaid."** Were these monies considered "contributions" or "loans"? I was not provided any loan documents or donation receipts supporting this claim. While this amount would cover the unallowable interest and penalties incurred, the Auditor did not find the necessary documentation to link these costs with the "contributions" or "loans" made by an officer of the Company.

7. **Hudson's management address in their plan to DCFS how they will repay their prior years' tax liability without using current period foster care funds.**

   Hudson's Proposed FCAP: See response to items #1.

   DCFS Response: This is not an acceptable plan. Please provide either loan documents or donations receipts reflecting the receipt of the "loan" or "contribution". In addition, supply ledger pages which show the receipt of the funds and the disbursement of them to pay prior years' tax liability.

8. **Hudson's management record the federal liability and any delinquent State taxes for which the Agency is ultimately found liable in the Agency's financial statements.**

   Hudson's Proposed FCAP: Please review the 2006 audited financial statement. These items have been properly addressed here.

   DCFS Response: DCFS has reviewed the 2006 audited financial statement, which brought a new issue to light. NOTE G – REIMBURSEMENTS DUE TO LACO states, "...Bearing interest at 10% and payable in monthly installments of $800..." At the present time, DCFS does not apply interest to repayment of overpayments.

9. **Hudson's management keep DCFS informed on the status of the State payroll tax issue until resolved.**

   Hudson's Proposed FCAP: Hudson Lyndsey will keep DCFS informed on the status of the State payroll tax issue until it is resolved.

   DCFS Response: Please submit quarterly Status reports beginning 7/30/08 for the quarter April – June 2008, 9/30/08 for the quarter July – September 2008, 1/30/09 for the quarter October – December 2008, and 4/30/09 for the quarter January – March 2009. Follow this report schedule until this issue is resolved.

10. **DCFS management work with Hudson's to resolve the overpayments and DCFS should collect any verified overpayments.**

    Hudson's Proposed FCAP: We are on a repayment plan of $800 per month. We will begin repayment immediately. As discussed in our exit meeting, there is still a discrepancy pertaining to a few children that were never in our care, nor did we receive payment on.

    DCFS Response: DCFS will have its Overpayment Collection Supervisor contact Hudson Lyndsey by 6/15/08 to schedule an appointment to reconcile DCFS records to Hudson Lyndsey's records. Once an overpayment balance is agreed upon, the agency must sign a new repayment agreement.

11. **Hudson's management ensure that any future payment discrepancies are immediately reported to DCFS and any overpaid amounts are repaid promptly.**

    Hudson's Proposed FCAP: Overpayments have recently been minimized, however, we will ensure when there is an overpayment identified, it will be returned timely.

    DCFS Response: DCFS will work with the agency to ensure this recommendation is implemented.

12. **Hudson's management require a second signature by an independent party on all checks where the payee and check signer are the same employee.**

    Hudson's Proposed FCAP: The following is Hudson Lyndsey's Board-approved policy and procedure requiring a second signature, by an independent party, on all checks where the payee and check signer are the same employee.

    Employees responsible for signing of checks shall ensure that the payee and check signer are never the same.

    DCFS Response: DCFS accepts the agency policy.

13. **Hudson's management ensure that checks are not made payable to cash.**

Hudson's Proposed FCAP: The following is an excerpt from Hudson Lyndsey's Board-approved policy and procedure manual addressing checks made payable to cash.

No checks shall be made payable to cash. Each authorized, and approved, request for payment form will reference the associated program expense and the payable party name.

DCFS Response: DCFS accepts the agency policy.

14. **Hudson's management establish written agreements for all loans indicating the amounts borrowed and the repayment terms.**

Hudson's Proposed FCAP: The following is an excerpt from Hudson Lyndsey's Board-approved policy and procedure manual addressing promissory notes.

All loans issued to Hudson Lyndsey will be preapproved by the Board. Once a short time loan has been approved a Promissory Note will be issued documenting the loan amount and terms of repayment. Interest is unallowable.

DCFS Response: DCFS accepts the agency policy.

15. **Hudson's management ensure that Los Angeles County warrants are deposited timely and consider having its County payments electronically deposited directly into the Agency's bank account.**

Hudson's Proposed FCAP: The following is an excerpt from Hudson Lyndsey's Board-approved policy and procedure manual addressing timely deposit of cash receipts. We will additionally consider electronic depositing, if approved by the Board.

Once cash receipts procedure has been completed, deposits will be make in a timely manner. Deposit are to be deposited daily prior to 4p.m. Any deposit not made on the day received shall be locked in the accounting department until the deposit is made the following day.

Smaller depositing, totaling under $500 can be held no later than Friday of the week received.

DCFS Response: DCFS accepts the agency policy.

16. **Hudson's management ensure that the Agency prepares monthly bank statement reconciliations which are prepared within 30 days of the bank statement date and that the reconciliations are signed and dated by the preparer.**

Hudson's Proposed FCAP: The following is an excerpt from Hudson Lyndsey's Board-approved policy and procedure manual addressing bank reconciliation.

It is policy of Hudson Lyndsey that all bank statements be reconciled with 30 days from the end of the month.

Statements shall be opened and reviewed prior to being submitted to the accounting department for reconciliation. All payees, endorsements and signers will be reviewed along with the statement.

Once the statement has been reconciled, it will be signed and dated and sent to management with the register for approval. No check will remain outstanding longer than 6 months. Stale dated checks shall be reviewed and cancelled or reissued as necessary.

DCFS Response: DCFS accepts the agency policy.

17. **Hudson's management review and cancel any checks that have not been negotiated within six months and reissue, if appropriate.**

Hudson's Proposed FCAP: See response to Recommendation #16.

DCFS Response: DCFS accepts the agency policy.

18. **Hudson's management maintain insurance coverage as required by the Contract.**

Hudson's Proposed FCAP: The following is an excerpt from Hudson Lyndsey's Board-approved policy and procedure manual addressing insurance coverage.

Insurance shall be maintained, without lapse, per the terms of the contract and any other insurance which is required in connection with the general conduct of business.

DCFS Response: Copy of certificate of general liability insurance received from DCFS Contract Management Services on May 30, 2008.

19. Hudson's management ensure that payments made to independent contractors are accurately reported on the 1099 Forms.

Hudson's Proposed FCAP: The following is an excerpt from Hudson Lyndsey's Board-approved policy and procedure manual addressing insurance coverage.

It is the responsibility of Hudson Lyndsey to properly document and report to all governing authorities 1099 contractors. All qualified 1099 independent contractors will meet the Internal Revenue Service guidelines as such.

DCFS Response: DCFS accepts the agency policy.

Skh
6/1/08

ATTACHMENT II

DCFS'S RESPONSE TO
HUDSON LYNDSEY FOSTER FAMILY AGENCY
FISCAL AUDIT

A-C AUDIT FINDINGS	COSTS ALLOWABLE BY DCFS	UNRESOLVED AMOUNT	COSTS UNALLOWABLE BY DCFS	DCFS' RESPOSE TO RECOMMENDATIONS TOTAL IN QUESTIONED COSTS $109,219
$ 73,939			$ 73,939	Unallowable Costs - Delinquent Payroll Taxes, Interest & Penalties
$ 6,250			$ 6,250	Unallowable Costs - NSF Overdraft Fees, Interest Charges and Late Fees
$ 24,667			$ 24,667	Inadequately Supported Credit Card Payments
$ 3,980			$ 3,980	Inadequately Supported Bank Account Withdrawls
$ 383			$ 383	Inadequately Supported Expenditure to Staples
$ 109,219		$ -	$ 109,219	

ORIGINAL QUESTIONED COSTS	$ 109,219
AMOUNT ALLOWED BY DCFS	$0
AMOUNT UNRESOLVED	$0
AMOUNT TO REPAID BY AGENCY**	$ 109,219

**To be determined at finalization of agency's FCAP.

Attachment III

DEPARTMENT OF CHILDREN AND FAMILY SERVICES
REPAYMENT SCHEDULE - HUDSON LYNDSEY FFA
FOR THE PERIOD OF 7/2008 THROUGH 6/2013

REPAYMENT SCHEDULE				
Payment No.	PERIOD MONTH	PERIOD YEAR	AMOUNT	BALANCE
			DISALLOWED COSTS:	$ 109,219.00
1	July	2008	$ 1,820.32	107,398.68
2	August	2008	$ 1,820.32	105,578.36
3	September	2008	$ 1,820.32	103,758.04
4	October	2008	$ 1,820.32	101,937.72
5	November	2008	$ 1,820.32	100,117.40
6	December	2008	$ 1,820.32	98,297.08
7	January	2009	$ 1,820.32	96,476.76
8	February	2009	$ 1,820.32	94,656.44
9	March	2009	$ 1,820.32	92,836.12
10	April	2009	$ 1,820.32	91,015.80
11	May	2009	$ 1,820.32	89,195.48
12	June	2009	$ 1,820.32	87,375.16
13	July	2009	$ 1,820.32	85,554.84
14	August	2009	$ 1,820.32	83,734.52
15	September	2009	$ 1,820.32	81,914.20
16	October	2009	$ 1,820.32	80,093.88
17	November	2009	$ 1,820.32	78,273.56
18	December	2009	$ 1,820.32	76,453.24
19	January	2010	$ 1,820.32	74,632.92
20	February	2010	$ 1,820.32	72,812.60
21	March	2010	$ 1,820.32	70,992.28
22	April	2010	$ 1,820.32	69,171.96
23	May	2010	$ 1,820.32	67,351.64
24	June	2010	$ 1,820.32	65,531.32
25	July	2010	$ 1,820.32	63,711.00
26	August	2010	$ 1,820.32	61,890.68
27	September	2010	$ 1,820.32	60,070.36
28	October	2010	$ 1,820.32	58,250.04
29	November	2010	$ 1,820.32	56,429.72
30	December	2010	$ 1,820.32	54,609.40
31	January	2011	$ 1,820.32	52,789.08
32	February	2011	$ 1,820.32	50,968.76
33	March	2011	$ 1,820.32	49,148.44
34	April	2011	$ 1,820.32	47,328.12
35	May	2011	$ 1,820.32	45,507.80
36	June	2011	$ 1,820.32	43,687.48
37	July	2011	$ 1,820.32	41,867.16
38	August	2011	$ 1,820.32	40,046.84
39	September	2011	$ 1,820.32	38,226.52
40	October	2011	$ 1,820.32	36,406.20
41	November	2011	$ 1,820.32	34,585.88
42	December	2011	$ 1,820.32	32,765.56
43	January	2012	$ 1,820.32	30,945.24

Payment No.	PERIOD MONTH	PERIOD YEAR	AMOUNT	BALANCE
44	February	2012	$ 1,820.32	29,124.92
45	March	2012	$ 1,820.32	27,304.60
46	April	2012	$ 1,820.32	25,484.28
47	May	2012	$ 1,820.32	23,663.96
48	June	2012	$ 1,820.32	21,843.64
49	July	2012	$ 1,820.32	20,023.32
50	August	2012	$ 1,820.32	18,203.00
51	September	2012	$ 1,820.32	16,382.68
52	October	2012	$ 1,820.32	14,562.36
53	November	2012	$ 1,820.32	12,742.04
54	December	2012	$ 1,820.32	10,921.72
55	January	2013	$ 1,820.32	9,101.40
56	February	2013	$ 1,820.32	7,281.08
57	March	2013	$ 1,820.32	5,460.76
58	April	2013	$ 1,820.32	3,640.44
59	May	2013	$ 1,820.32	1,820.12
60	June	2013	$ 1,820.12	(0.00)