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April 29, 2004

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

From: J. Tyler McCauley
Auditor-Controller

Subject: **FISCAL REVIEW OF CONCEPT 7 FOSTER SUPPORT & TREATMENT CENTERS - A FOSTER FAMILY AGENCY CONTRACTOR**

Attached is our audit report on Concept 7 Foster Support & Treatment Centers (Concept 7 or Agency) fiscal operations for the period of January 1, 2002 through December 31, 2002. The Agency is licensed to operate a Foster Family Agency (FFA) and for the period of our review, had 198 children placed by Los Angeles County in approximately 115 certified homes. During the period of our review, the Agency received $3,484,312 in FFA funds from the Department of Children and Family Services (DCFS) and paid $1,612,458 of the FFA funds directly to foster parents. Concept 7's administrative office is located in Orange County, but has offices located in the First and Fifth Supervisorial Districts.

Scope

The purpose of our review was to determine whether Concept 7 has 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 fiscal guidelines governing the disbursement of FFA foster care funds. Our review was conducted at the request of DCFS.

Summary of Findings

Our review disclosed a total of $42,185 in questioned costs and unaccounted for revenue. Concept 7 needs to strengthen its internal controls over fixed assets, disbursements, and bank reconciliations. Concept 7 also invested FFA funds in a money market account which is not insured by the FDIC and where there is a risk of loss of funds.

We have recommended that DCFS resolve the questioned costs and, if appropriate, collect all disallowed amounts. In addition, DCFS needs to ensure that the Agency's management takes the appropriate corrective actions to address the recommendations in this report and monitor to ensure that the corrective actions taken result in permanent changes.

Review of Report

We discussed our report with Concept 7 management on March 8, 2004. The Agency's management has agreed to provide DCFS with a written response and corrective action plan within 30 days of this report. 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 Concept 7's management and staff for their cooperation during our review.

If you have any questions, please contact me, or have your staff contact DeWitt Roberts at (626) 293-1101.

JTM:DR:MM
Attachment

c: Chief Administrative Office
David E. Janssen, Chief Administrative Officer
Claudine Crank, Budget & Operations Management Branch
Raymond Fortner, Interim County Counsel
Department of Children and Family Services
David B. Sanders, Ph.D., Director
Angela Carter, Deputy Director, Bureau of Administration
Joan Smith, Deputy Director, Bureau of Finance
Edward Sosa, Interim Division Chief, Quality Assurance Division
Concept 7 Family Support & Treatment Centers
Marlene Mills-Margesson, 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
Violet Varona-Lukens, Board of Supervisors Executive Office
Public Information Office
Audit Committee Members
Commission for Children and Families

CONCEPT 7 FAMILY SUPPORT AND TREATMENTS CENTERS
FISCAL AUDIT OF FOSTER FAMILY AGENCY CONTRACT

BACKGROUND

The Department of Children and Family Services (DCFS) contracts with Concept 7 Family Support & Treatment Centers (Concept 7 or Agency) to recruit, certify, train and support foster family homes and to provide treatment and support services for DCFS children placed in these homes. For the period of our review, January 1, 2002 through December 31, 2002, Concept 7 had 198 children placed by Los Angeles County in approximately 115 certified homes. Concept 7's administrative office is located in Orange County, but it has offices in the First and Fifth Supervisorial Districts.

Under the provisions of the contract, DCFS pays Concept 7 a monthly rate based on the FFA Treatment Rate Notification Letter provided by the California Department of Social Services (CDSS). During our review period, the Agency received a monthly rate between $1,589 and $1,865 per foster child. For our review period, the Agency received $3,484,312 in foster care funds from DCFS.

CDSS has also established minimum amounts that Concept 7 is required to pay certified foster parents. Concept 7 is required to pay the foster parents between $624 and $790 per month in accordance with the CDSS minimum rate criteria. During the period of our review, Concept 7 paid out approximately $1,612,458 to foster parents.

APPLICABLE REGULATIONS AND GUIDELINES

Concept 7 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 D, DCFS' Contract Accounting and Operating Handbook (DCFS Handbook)

- Federal Office of Management and Budget Circular A-122, Cost Principles for Non-Profit Organizations (Circular A-122)

- California Department of Social Services Manual of Policies and Procedures (CDSS MPP)

- California Code of Regulations, Title 22 (Title 22)

REVIEW OF EXPENDITURES/REVENUES

Our review disclosed a total of $42,185 in questioned costs and unaccounted for revenue. Details of these costs/revenues are discussed below.

Unsupported/Inadequately Supported Costs

The DCFS 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.

Concept 7 did not have itemized receipts or invoices to support foster care expenditures totaling $16,646. Specifically we noted:

- $13,418 in unsupported expenditures for items such as conferences, an airline ticket, moving and storage fees, a travel agency fee, Nordstrom's, a hotel room, and restaurants.

- $3,228 in inadequately supported expenditures for items such as seminars, petty cash reimbursements, rent, hotels, and restaurants.

Employee Bonuses

The Circular A-122 states that compensation for services shall be made for reasonable and actual personal services, rather than a distribution of earnings in excess of costs. Concept 7 paid $22,258 in bonuses to its employees. Concept 7 management stated that it has an established policy of awarding additional compensation to employees at year-end when funds are available. When we requested to see the policy, Concept 7 management stated that the policy is not in writing.

Unallowable Costs

Personal Expenditures

Concept 7 used FFA funds for unallowable costs totaling $1,449. These costs all relate to an October 2002 Board of Directors retreat and include $684 in hotel room costs, $598 in meals expenses and $167 in expenses for alcoholic beverages.

- The hotel room costs were for three Concept 7 employees. The hotel (which was also the location of the retreat) is located less than 11 miles from the Agency's headquarters. Accordingly, the hotel stay appears to have been for convenience purposes.

- According to Agency records, 13 people attended the retreat, yet 15 breakfasts, 15 lunches and 24 dinners were paid for. To the extent more meals were paid for than there were attendees, we are questioning the cost of the meals.

The DCFS Handbook Section 1.3 states that only those expenditures that are necessary, proper and reasonable to carry out the purposes and activities of the Program are allowable.

- A total of $167 in alcoholic beverages were paid for using foster care funds. The Circular A-122 states that the cost of alcoholic beverages is unallowable.

Unaccounted for Revenue

For the period of January 1, 2002 through December 31, 2002, we attempted to trace payments made by DCFS to Concept 7's bank records (i.e., deposit slips and bank statements). We were unable to trace $1,832 in DCFS payments to Concept 7's bank account. As a result, we were unable to determine if the funds were used for allowable FFA activities.

Recommendations

DCFS management:

1. **Resolve the $42,185 in questioned costs and unaccounted for revenue and, if appropriate, collect any disallowed amounts.**

Concept 7 management:

2. **Consistently maintain adequate supporting documentation for all foster care expenditures, including original itemized receipts/invoices.**

3. **Ensure employee bonuses are made in accordance with Circular A-122.**

DCFS Overpayments

As of December 2002, Concept 7's financial statements indicated $47,838 "Due to L.A. County for Overpayments." The Agency's financial statements indicated that some of these overpayments originated during calendar years 2000 and 2001. Concept 7 management indicated that it has been working with DCFS to resolve these overpayment amounts. However, DCFS was not able to confirm the validity of selected overpayments included in Concept 7's overpayment balance and indicated that they would not be able to do so without significant additional research. Concept 7's accounting records also reflected $204,652 in unresolved underpayments. Concept 7 and DCFS management need to work together to resolve these over/underpayments.

Recommendation

4. **DCFS management and Concept 7 resolve the overpayments and underpayments and monitor to ensure that over/underpayments are resolved timely.**

Investment of Foster Care Funds

According to the Circular A-122, investing funds where the outcome of the investment is uncertain is not allowable. As of December 31, 2002, the Agency had a total of $284,991 invested in a money market account, which is not FDIC insured. The account's prospectus clearly states that it is possible to lose money by investing in the fund.

While we were not able to determine what portion of the invested funds were County funds, we noted that approximately 46% of the Agency's revenues were received from the County. Accordingly, it is likely that a significant portion of the funds invested in mutual funds were originally received from the County. Therefore, Concept 7 should discontinue its practice of investing County foster care funds in investments where there is a risk of loss.

Recommendation

5. **Concept 7 management discontinue the practice of investing County foster care funds in investments where there is a potential risk of loss.**

Contract Compliance and Internal Controls

Our review disclosed several contract compliance issues and internal control weaknesses in addition to those already mentioned. DCFS should ensure that Concept 7 management takes appropriate corrective actions to address each of the internal control recommendations in this report. DCFS should also monitor this contractor to ensure that these corrective actions result in permanent changes.

Accounting Procedures

We reviewed Concept 7's accounting procedures and noted:

- DCFS 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. We reviewed Concept 7's timeliness of depositing DCFS payments and noted several instances where the Agency made deposits for amounts over $500 up to 15 days after the check issue date. The Agency needs to take steps to ensure that deposits of County payments are made timely. Many FFA's that contract with the County have their County payments direct deposited. To ensure timely deposits and increase security over payments, Concept 7 should consider direct deposits to improve the timeliness of its County payment deposits.

- It was not possible to trace fixed assets purchased by Concept 7 to the actual location of the asset as recorded on Agency's fixed asset records. DCFS Handbook Section 4.2 states that agencies shall maintain a current listing of fixed assets, including the item description, serial number, date of purchase, acquisition cost and sources of funding. The Agency provided us with two different fixed asset listings. The first listing contained a description of the item along with the purchase date and depreciation amounts. The second listing contained a description of the item, its location and an internal asset identification number. However, assets were only traceable from source documentation such as invoices and receipts to the first listing. The descriptions of the assets varied between the two listings, resulting in our being unable to reconcile the two listings to one another to ascertain an asset's identification number, and ultimately the asset's physical location.

Recommendations

Concept 7 management:

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

7. **Maintain one fixed asset listing that includes the item description, purchase date, serial number, acquisition cost, asset location, funding source and depreciation amounts in compliance with the DCFS Handbook.**

Disbursement Procedures

The Agency's disbursement procedures need to be strengthened to minimize the chance of FFA funds being used to pay for non-FFA expenses.

Our review of Concept 7's credit card charges disclosed that the Executive Director charged $1,257 in personal expenses to the Agency's American Express card. Although the Executive Director subsequently reimbursed the Agency in a timely manner, the Agency's credit card should only be used to conduct Agency business. In addition, we noted several instances in which the Executive Director authorized, signed, and issued payments to herself. To ensure proper accountability and control over the Agency's funds, Concept 7 should require someone such as the Chief Financial Officer, or a Board member (i.e., someone not considered to be an "interested person" under section 5227 of the Corporations Code), to review and approve all checks written to American Express or to the Executive Director.

Recommendations

Concept 7 management:

8. **Discontinue its current policy which allows the Executive Director to use the Agency's American Express card for personal use.**

9. **Ensure that the Chief Financial Officer, or a Board member (i.e., someone not considered to be an "interested person" as defined in section 5227 of the Corporations Code) review and approve all checks written to American Express, or to the Executive Director.**

Bank Reconciliations

DCFS Handbook Section 4.011 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. Concept 7 does not sign and date its bank reconciliations. Therefore, we were unable to determine whether the bank reconciliations were prepared timely and reviewed for appropriateness and accuracy.

Recommendation

10. **Concept 7 management ensure the Agency's bank account reconciliations are signed and dated by both the preparer and the reviewer**.