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GOVERNOR

September 25, 2012

FOSTER CARE AUDITS and RATES LETTER (FCARL) NO. 2012-01

TO: ALL GROUP HOME PROVIDERS
ALL FOSTER FAMILY AGENCIES
ALL COMMUNITY TREATMENT FACILITY PROVIDERS
ALL COUNTY WELFARE DIRECTORS
ALL COUNTY CHIEF PROBATION OFFICERS
ALL MENTAL HEALTH DIRECTORS

SUBJECT: REVISED FISCAL AUDIT PROTOCOLS

Enclosed are the most current protocols for fiscal audits performed of non-profit organizations (NPOs) that receive Title IV-E, Aid to Families with Dependent Children-Foster Care (AFDC-FC) funds to operate foster care programs, including group homes and/or Foster Family Agencies. These protocols are used by the California Department of Social Services (CDSS) Foster Care Audits and Rates Branch's auditors who perform fiscal audits, and supersede those previously updated in March 2007.

Pursuant to Welfare and Institutions Code section 11466.2(a)(1), CDSS is required to perform or have performed fiscal audits of foster care providers. Therefore, fiscal audit protocols have been revised and updated to reflect current practices. In addition, this FCARL is being issued to provide guidance to NPOs regarding preparation for a fiscal audit.

Purpose of a Fiscal Audit

The purpose of a fiscal audit is to evaluate the financial condition of an NPO that receives AFDC-FC funds to provide foster care services to children in out-of-home care, to determine whether the program funds were spent on allowable and reasonable costs, that expenditures have the appropriate documentation, and that the NPO complies with all applicable state and federal laws and regulations related to the program operations. The applicable laws and regulations include, but are not limited to, the California Corporations Code (CCC), the Manual of Policies and Procedures (MPP), Generally Accepted Government Audit Standards (GAGAS), and federal Office of Management and Budget (OMB) Circular A-133 Auditing Standards and OMB A-122 Cost Principles.

Preparing for a Fiscal Audit

Each NPO should ensure that the records for their program(s) are clear, concise, maintained separately from other program operations, well-organized and are made available to the CDSS Auditor(s). NPOs shall maintain program records for a minimum of five (5) years. Also, program expenditures should be well-documented and indicate the purpose for each transaction. The better prepared you are for the audit, the more efficiently and smoothly the audit will proceed. The CDSS Auditor(s) will request and review records for the AFDC-FC program related to internal controls, financial records, and the Board of Directors. It is **NOT** the responsibility of the Auditor(s) to reconstruct records. If the NPO does not have sufficient records, the Auditor(s) will make a determination based on the records available.

Helpful Hints for the Review of Records

Each NPO should be familiar with the appropriate federal and state laws, regulations, and be prepared to provide program records, such as, but not limited to:

- OMB Circular A-122 Cost Principles (Attachment A and B);
- MPP state regulations for Reporting Allowable Costs (MPP Section 11-402.82);
- NPO's Policies and Procedures Manual;
- Board of Directors Minutes and Resolutions;
- Board of Director's Statement(s) (LIC-9165) located on page iii of the "Facts You Need to Know, Group Home Board of Directors" booklet;
- Articles of Incorporation;
- Bylaws and amendments, if applicable;
- Return of Organization Exempt From Income Tax (Form 990);
- General Ledger and Check Register;
- Contractual agreements (i.e. professional services, consultants, etc.);
- Loan Agreements, etc.;
- Receipts and invoices;
- Bank statements and reconciliations;
- Cash withdrawals;
- Petty cash disbursements;
- Cancelled business checks;
- Lease agreements (building, land, vehicle);
- Executive salaries and fringe benefits;
- Expense reimbursements;
- Credit card purchases, if applicable;
- Accounts payables/receivables;
- Utilities (cell phone, electric, gas, etc.);
- Maintenance and repairs;
- Training and Travel;
- Automobile Expenses (Car Allowances, Mileage Reimbursements, etc.); and
- Fines and Penalties.

In addition, each NPO should ensure that internal controls for program operations are adequate and are appropriately followed in areas, such as, but not limited to:

- Separation of duties;
- Proper authorization of expenditures;
- Costs are appropriately applied to the AFDC-FC program;
- Contracts are properly recorded, documented and comply with applicable regulations; and
- Original receipts match expenditures; identify the business purpose; and in some cases, reflect Board of Directors approval.

If you have any questions regarding the information contained in this FCARL letter, please contact Mr. B. Ray Thomas, Audit Manager, or Ms. Fanita Polk-Reaves, Manager, Audits Policy and Support Unit, at (916) 653-1802.

Sincerely,



CORA L. DIXON, Acting Chief
Foster Care Audits and Rates Branch

Enclosure

- c: California Alliance of Child and Family Services
Community Residential Care Association of California
California Welfare Directors Association
Angela Valdez, Program Administrator,
Community Care Licensing, MS 8-3-54

NON-PROFIT ORGANIZATION
FISCAL AUDIT PROTOCOLS
(FOSTER CARE GROUP HOME AND FOSTER FAMILY AGENCY)
August 2012

The purpose of the fiscal audit is to evaluate the financial condition of non-profit organizations (NPO) providing foster care group home (GH) and foster family agency (FFA) services, in accordance with applicable Manual of Policies and Procedures (MPP), Generally Accepted Government Auditing Standards (GAGAS), and Office of Management and Budget (OMB) Circular A-122 cost principles and OMB Circular A-133 auditing standards.

I. PREPARATION AND PLANNING

Pre-field planning and preparation is crucial to an efficient and professional audit. The more thorough and comprehensive the planning, the more smoothly the audit will proceed.

A. Initiation

Fiscal audits are initiated for the California Department of Social Services (CDSS) Program and Financial Audits Bureau (PFAB), based on referrals from a variety of sources including, but not limited to, Financial Audits Unit (FAU); CDSS Community Care Licensing (CCL); County Placement Agencies; Program/Provisional Audits Unit; the Foster Care Rates Bureau (FCRB); current or former GH and FFA employees; and, the public or interested parties. In addition, fiscal audits can also be initiated by CDSS' random selection process.

B. Processing and Evaluating Referrals

Referrals from the FAU, CCL, Program/Provisional Audits Unit, and the FCRB

1. Referrals from the above sources are transmitted via email or hard copy to the Foster Care Audits Policy and Support Manager for intake and tracking purposes.

2. Referrals from the FAU will be in a monthly list of high risk ratings resulting from desk reviews of Financial Audit Reports prepared by Certified Public Accountants.

Outside Referrals (from any source other than CDSS)

Referrals received from outside CDSS are forwarded to the Policy and Support Unit Manager for intake and tracking purposes. After entry into the tracking system, referrals will be forwarded to the Audit Manager.

C. Preliminary Audit Planning

1. The Audit Manager will review the referral to determine whether a fiscal audit appears warranted. If so, then the referral will be assigned to an auditor who will begin the Preliminary Audit Planning.
2. Upon receipt of the audit assignment, the Auditor-in-Charge (AIC)/auditor will gather and analyze background information. This information includes but is not limited to:
 - a. Review the Financial Audits Unit files of the NPO;
 - b. Contact the appropriate Rates Consultant and review the NPO rates file including Board of Directors signed acknowledgement of duties;
 - c. Contact the CCL Analyst for background information.
 - d. Review any prior audit reports: i.e., CDSS provisional/non provisional audits, Los Angeles County Auditor-Controller audits;
 - e. Obtain the Agent for Service of Process from the Secretary of State's website at www.ss.ca.gov and if available, obtain a copy of the "Return of Organization Exempt From Income Tax," (Form 990) from the Attorney General's website at www.ag.ca.gov;
 - f. Contact the complainant about the referral, if deemed necessary; and
 - g. Document all contacts on the Fiscal Audit Contact Log sheet.

3. The AIC/auditor will meet with the Audit Manager to discuss the background information gathered and determine if the audit is still warranted.
 - a. If the audit is warranted the Audit Manager may assign additional audit staff, as necessary.
 - b. If the audit is not warranted the Audit Manager will document the reason(s) in the file for not conducting the audit and notify the Policy and Support unit Manager for tracking.

D. Scheduling and Pre-field Preparation

1. The Audit Manager will contact the NPO by phone to schedule the audit. This phone call should be made at least 35 days in advance of the audit so that the confirmation letter can be mailed 30 days prior to the field audit. During the phone call, the Audit Manager will:
 - a. Introduce himself/herself and explain the reason for the phone call;
 - b. Confirm date(s), time(s), and place of audit;
 - c. Establish where the audit will be conducted; at the corporate headquarters, or at a separate administrative office;
 - d. Explain the purpose, scope, and methodology;
 - e. Identify the audit period based on the corporation's fiscal year;
 - f. Identify records to be reviewed for the audit period;
 - g. Explain to the NPO that they must have all the necessary documents available at the agreed upon location;
 - h. Explain that a written confirmation letter will be sent; and
 - i. Document the phone call on the Fiscal Audit Contact Log sheet.
2. The AIC will follow up with a phone call and send a written Scheduling Letter at least 30 days prior to the initiation of the

field visit. The letter must be signed by the Bureau Chief and contain the following:

- a. The date of the initial phone call and person contacted;
 - b. Date, time and place of audit;
 - c. Name of the AIC;
 - d. Purpose and Scope of the audit;
 - e. Audit period; and
 - f. List of documents to be reviewed during the audit.
3. The audit scheduling letter must be sent to the Agent for Service of Process and the President of the Board of Directors with a copy to the Executive Director. Copies must be sent to the Managers of the Audits Policy and Support Unit, FCRB and Program/Provisional Audits Units; CCL Program Analyst; and primary placing agencies. One copy should be retained for the official audit file.
4. Prior to the start of the field audit, the AIC will contact the NPO again to ensure that the necessary records are available, and answer any questions the NPO may have concerning the audit.
5. Establish an official audit file. At a minimum, the file should contain the following sections:
- a. Preliminary Audit Planning
 - Audit Planning - includes Planning Memorandum, Audit Checklist, Correspondence/Audit Contact Log, and Scheduling Letter. All contacts should be logged by date, name, and subject, and initialed by the auditor.
 - Referral Information-includes the incoming referral documentation and the analysis of the documentation.
 - Financial Review Information-Includes copies of the Financial Audit Report (FAR) and/or relevant records and analysis.

- Preliminary FCRB-includes the program statement, applicable rate application(s), and copies of any pertinent Rates correspondence.
- Prior Program/Provisional Audit Reports-the most recent program or provisional audit report as applicable.
- Preliminary Audit/CCL Review-includes all information received from CCL including LIS records.

b. Field Work

- Entrance Conference-includes Entrance Questionnaire, Organization chart, and any other records received at the entrance conference.
- Internal Controls-includes Internal Control Questionnaire and staff interview worksheets.
- Expenditures-includes general ledger, check registers, invoices, bank statements, receipts, etc., and applicable copies of NPO's accounting records.
- Board of Directors-includes Board of Directors Questionnaire, board minutes, bylaws, resolutions, and interviews.
- Exit Conference-includes summary of Exit Conference, point sheets, and any other relevant records.

c. Post Field Work

- Report Section-includes draft of Management Decision Letter (MDL), final MDL, and other documents.
- Quality Control-includes Quality Control (QC) documents and review notes.

d. Administrative Review

- Formal Hearing-includes request for hearing (Statement of Disputed Audit Findings), notice of hearing date, legal briefs, proposed decisions, stipulations and waivers, adopted decisions and orders, and revised calculation(s), if applicable.

6. Before field work, the AIC, audit team, and audit manager will meet to discuss pre-audit planning, travel arrangements, and field work assignments.
7. The audit manager reviews and approves the planning and budget for each specific audit.

II. **FIELD WORK**

A. Entrance Conference

The AIC and audit staff will conduct a formal Entrance Conference with the NPO staff. During the Entrance Conference, the AIC will:

1. Introduce audit staff and establish a professional working relationship with the NPO;
2. Discuss the purpose of the audit, the scope, methodology, and time frames;
3. At a minimum, obtain the following information for the audit period:
 - a. The number and types of programs operated by the NPO;
 - b. The primary activities or services provided by each program;
 - c. The sources of funding for all programs;
 - d. The NPOs Internal Control policies and procedures; and
 - e. Respond to any other questions/concerns identified by the NPO.

B. Review of Records

1. Internal Controls

a. Auditors will review NPO's Accounting and Internal Control Procedures, interview key staff, and complete an Internal Control Questionnaire. Perform tests to evaluate the effectiveness of Internal Controls and ensure compliance with applicable auditing standards, which may include, but not be limited to, testing transactions from any of the following areas:

- Cash, Cash Receipts, and Disbursements
- Credit Card purchases
- Accounts Payable/Receivable
- Petty Cash
- Bank Reconciliations
- Payroll Disbursements
- Assets
- Leases (building, land, vehicle, etc.), and
- Loan Agreements/Notes Payable
- Contracts

2. Expenditures

a. Auditors will review NPO's accounting records to determine if AFDC-FC funds are spent on allowable and reasonable costs, in accordance with OMB Circular A-122 cost principles, and if expenditures are supported and well-documented indicating the purpose for each transaction. The review of expenditures will include an evaluation of all transactions for selected cost item(s), such as, but not limited to:

- Credit Card purchases
- Car Allowances
- Loans

- Expense Reimbursements
- Bonuses
- Executive Salaries and Fringe Benefits
- Consulting Fees
- Rent/Lease Obligations
- Travel and Entertainment
- Maintenance and repairs
- Utilities
- Professional services
- Training
- Meetings and Conferences
- Equipment and capital expenditures
- Fines and Penalties
- Miscellaneous

3. Board of Directors

Pursuant to the California Corporations Code, auditors will review the composition and validity of the Board of Directors based on the Articles of Incorporation, Bylaws, amendments, and all applicable records. These records, include, but are not limited to the Board Minutes, resolutions, and Board of Director Statements (LIC-9165), etc. The auditors will interview key Board members to determine their role in overseeing the NPO's program operations.

C. Concluding the Field Work

1. Once all pertinent records have been reviewed, analyzed, and appropriate working papers completed, the auditors will make a preliminary determination regarding the NPO's program operations.

2. The AIC will discuss the preliminary findings, if any, with the Audit Manager prior to taking any further action.

D. Exit Conference

The AIC, audit team, and/or Audit Manager will conduct a formal Exit Conference at the conclusion of the field work. At that time, the AIC and/or Audit Manager will:

1. Present an overview of the audit and provide a copy of the point sheets, detailing the findings, and reasons for each finding.
2. Explain the report issuance process, identify timelines, which includes a 15-calendar day follow-up period to submit additional documentation for review.
3. Explain the appeal process, corrective action requirements, and repayment of any unallowable and/or disallowed costs, if applicable.
4. Complete the Fiscal Audit Summary of Exit Conference form, respond to the NPO's questions, and obtain the NPO's representative's signature.

III. POST FIELD WORK AND MANAGEMENT DECISION LETTERS

A. Final Management Decision Letter (MDL)

The AIC will allow 15 calendar days from the date of the Exit Conference for the NPO to submit additional documentation, during which the AIC will start to develop a draft of the final MDL containing all the findings and instructions for any necessary corrective action. The AIC will incorporate the NPO's response/additional documentation submitted.

1. The draft of the final MDL and audit workpapers will be submitted to the Audit Manager for supervisory review.
2. Upon completion, the draft of the final MDL will undergo the internal QC process, be finalized and routed for signature by the Bureau Chief.
3. The original copy of final MDL will be sent to the Agent for Service of Process, with additional copies to the President of the Board of Directors, the Executive Director, and county placing agencies. One copy should be retained for the official audit file.

B. Corrective Action

The NPO has 60 days from the date of the final MDL to comply with identified corrective action. Evidence that corrective action has been achieved will be supported by the NPO submitting adequate documentation regarding the specific recommendations identified in the final MDL. Failure to substantially comply with expected corrective actions may result in the termination of **all** of the NPO's program rate(s).

C. Appeals Process

1. The NPO has the right to file an appeal regarding any audit findings identified in the final MDL within 30 days of issuance. The appeal will be heard in a formal hearing within 60 days of receipt of the request for hearing. If the NPO does not file an appeal, the audit findings in the final MDL are considered final and any unallowable and/or disallowed costs would be sustained and collectible.
2. The CDSS' PFAB will track the timeline for appeals and collections activities.

IV. OUTSIDE REFERRALS

- A. The CDSS may make referrals to other entities including the Attorney General's Office, District Attorney, United States Attorney's Office, Internal Revenue Service (IRS), Franchise Tax Board (FTB), Charitable Trust, etc. for significant material findings, egregious misuse of funds, and/or severe lack of board oversight.
- B. In all cases, referrals to an outside agency must be reviewed and approved by CDSS' Foster Care Audits and Rates Branch Chief and Legal before being made.