SANTA CLARA COUNTY

Audit Report

CONSOLIDATED HANDICAPPED AND DISABLED STUDENTS (HDS), HDS II, AND SEDP PROGRAM

Chapter 1747, Statutes of 1984; Chapter 1274, Statutes of 1985; Chapter 1128, Statutes of 1994; and Chapter 654, Statutes of 1996

July 1, 2006, through June 30, 2010

JOHN CHIANG
California State Controller

October 2014

JOHN CHIANG
California State Controller

October 21, 2014

The Honorable Mike Wasserman, President
Board of Supervisors
Santa Clara County
70 W. Hedding St., 10th Floor
San Jose, CA 95110

Dear Mr. Wasserman:

The State Controller's Office audited the costs claimed by Santa Clara County for the legislatively mandated Consolidated Handicapped and Disabled Students (HDS), HDS II, and SEDP Program (Chapter 1747, Statutes of 1984; Chapter 1274, Statutes of 1985; Chapter 1128, Statutes of 1994; and Chapter 654, Statutes of 1996) for the period of July 1, 2006, through June 30, 2010.

The county claimed $7,396,444 for the mandated program. Our audit found that the entire amount is unallowable because the county overstated assessment and treatment costs, claimed duplicate costs, overstated residential placement costs, overstated related indirect costs, and understated offsetting reimbursements. The State paid the county $1,931,987, which the State will offset from other mandated program payments due the county. Alternatively, the county may remit this amount to the State.

If you disagree with the audit findings, you may file an Incorrect Reduction Claim (IRC) with the Commission on State Mandates (Commission). The IRC must be filed within three years following the date that we notify you of a claim reduction. You may obtain IRC information at the Commission's website at www.csm.ca.gov/docs/IRCForm.pdf.

If you have any questions, please contact Jim L. Spano, Chief, Mandated Cost Audits Bureau, by phone at (916) 323-5849.

Sincerely,

Original signed by

JEFFREY V. BROWNFIELD, CPA
Chief, Division of Audits

JVB/mh

Attachment

cc: Emily Harrison, Director of Finance, Finance Agency
Santa Clara County
Kim-Anh Le, CPA, Division Manager, Finance Agency
Santa Clara County
Greta Hansen, Lead Deputy County Counsel,
Santa Clara County
Kavita Narayan, Deputy County Counsel
Santa Clara County
Michael Byrne, Principal Program Budget Analyst
Mandates Unit, Department of Finance
Carol Bingham, Senior Fiscal Policy Advisor
Government Affairs Division
California Department of Education
Erika Cristo
Special Education Program
California Department of Mental Health
Chris Essman, Manager
Special Education Division
California Department of Education
Jay Lal, Manager
Division of Accounting and Reporting
State Controller's Office

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Audit Report

Summary

The State Controller's Office (SCO) audited the costs claimed by Santa Clara County for the legislatively mandated Consolidated Handicapped and Disabled Students (HDS), HDS II, and SEDP Program (Chapter 1747, Statutes of 1984; Chapter 1274, Statutes of 1985; Chapter 1128, Statutes of 1994; and Chapter 654, Statutes of 1996) for the period of July 1, 2006, through June 30, 2010.

The county claimed $7,396,444 for the mandated program. Our audit found that the entire amount is unallowable because the county overstated assessment and treatment costs, claimed duplicate costs, overstated residential placement costs, overstated related indirect costs, and understated offsetting reimbursements. The State paid the county $1,931,987, which the State will offset from other mandated program payments due the county. Alternatively, the county may remit this amount to the State.

Background

Handicapped and Disabled Students (HDS) Program

Chapter 26 of the Government Code, commencing with section 7570, and Welfare and Institutions Code section 5651 (added and amended by Chapter 1747, Statutes of 1984, and Chapter 1274, Statutes of 1985), require counties to participate in mental health assessment for "individuals with exceptional needs," participate in the expanded "Individualized Education Program" (IEP) team, and provide case management services for "individuals with exceptional needs" who are designated as "seriously emotionally disturbed." These requirements impose a new program or higher level of service on counties.

On April 26, 1990, the Commission on State Mandates (Commission) adopted the statement of decision for the HDS Program and determined that this legislation imposed a State mandate reimbursable under Government Code section 17561. The Commission adopted the parameters and guidelines for the HDS Program on August 22, 1991, and last amended them on January 25, 2007.

The parameters and guidelines for the HDS Program state that only 10% of mental health treatment costs are reimbursable. However, on September 30, 2002, Assembly Bill 2781 (Chapter 1167, Statutes of 2002) changed the regulatory criteria by stating that the percentage of treatment costs claimed by counties for fiscal year (FY) 2000-01 and prior fiscal years is not subject to dispute by the SCO. Furthermore, this legislation states that, for claims filed for FY 2001-02 and thereafter, counties are not required to provide any share of these costs or to fund the cost of any part of these services with money received from the Local Revenue Fund established by Welfare and Institutions Code section 17600 et seq. (realignment funds).

Furthermore, Senate Bill 1895 (Chapter 493, Statutes of 2004) states that realignment funds used by counties for the HDS Program "are eligible for reimbursement from the state *for all allowable costs* to fund

assessments, psychotherapy, and other mental health services . . ." and that the finding by the Legislature is "declaratory of existing law" (emphasis added).

The Commission amended the parameters and guidelines for the HDS Program on January 26, 2006, and corrected them on July 21, 2006, allowing reimbursement for out-of-home residential placements beginning July 1, 2004.

Handicapped and Disabled Students II (HDS II) Program

On May 26, 2005, the Commission adopted a statement of decision for the HDS II Program that incorporates the above legislation and further identified medication support as a reimbursable cost, effective July 1, 2001. The Commission adopted the parameters and guidelines for this new program on December 9, 2005, and last amended them on October 26, 2006.

The parameters and guidelines for the HDS II Program state that "Some costs disallowed by the State Controller's Office in prior years are now reimbursable beginning July 1, 2001 (e.g., medication monitoring). Rather than claimants re-filing claims for those costs incurred beginning July 1, 2001, the State Controller's Office will reissue the audit reports." Consequently, we are allowing medication support costs commencing on July 1, 2001.

Seriously Emotionally Disturbed Pupils (SEDP) Program

Government Code section 7576 (added and amended by Chapter 654, Statutes of 1996) requires new fiscal and programmatic responsibilities for counties to provide mental health services to seriously emotionally disturbed pupils placed in out of state residential programs. Counties' fiscal and programmatic responsibilities include those set forth in Title 2, *California Code of Regulations*, section 60100, which provides that residential placements may be made out-of-state only when no in-state facility can meet the pupil's needs.

On May 25, 2000, the Commission adopted the statement of decision for the Seriously Emotionally Disturbed Pupils (SEDP): Out-of-State Mental Health Services Program and determined that Chapter 654, Statutes of 1996, imposes a State mandate reimbursable under Government Code section 17561. The Commission adopted the parameters and guidelines for the SEDP Program on October 26, 2000. The Commission determined that the following activities are reimbursable:

- Payment for out-of-state residential placements;
- Case management of out-of-state residential placements. Case management includes supervision of mental health treatment and monitoring of psychotropic medications;
- Travel to conduct quarterly face-to-face contacts at the residential facility to monitor level of care, supervision, and the provision of mental health services as required in the pupil's IEP; and

- Program management, which includes parent notifications as required; payment facilitation; and all other activities necessary to ensure that a county's out-of-state residential placement program meets the requirements of Government Code section 7576.

The Commission consolidated the parameters and guidelines for the HDS, HDS II, and SEDP Programs for costs incurred commencing with FY 2006-07 on October 26, 2006, and last amended them on September 28, 2012. On September 28, 2012, the Commission stated that Statutes of 2011, Chapter 43, "eliminated the mandated programs for counties and transferred responsibility to school districts, effective July 1, 2011. Thus, beginning July 1, 2011, these programs no longer constitute reimbursable State-mandated programs for counties." The consolidated program replaced the prior HDS, HDS II, and SEDP mandated programs. The parameters and guidelines establish the State mandate and define reimbursable criteria. In compliance with Government Code section 17558, the SCO issues claiming instructions to assist local agencies and school districts in claiming mandated program reimbursable costs.

Objectives, Scope, and Methodology

We conducted the audit to determine whether costs claimed represent increased costs resulting from the Consolidated Handicapped and Disabled Students (HDS), HDS II, and SEDP Program for the period of July 1, 2006, through June 30, 2010.

The objectives of our audit were to determine whether costs claimed were supported by appropriate source documents, were not funded by another source, and were not unreasonable and/or excessive.

The legal authority to conduct this audit is provided by Government Code sections 12410, 17558.5, and 17561. We did not audit the county's financial statements. We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

We limited our review of the county's internal controls to gaining an understanding of the transaction flow and claim preparation process as necessary to develop appropriate auditing procedures. Our audit scope did not assess the efficiency or effectiveness of program operations.

To achieve our audit objectives, we performed the following audit procedures:

- Interviewed employees, completed the internal control questionnaire, and performed a walk-through of the cost components of each claim.

- Traced costs claimed to supporting documentation that showed when the costs were incurred, the validity of such costs, and their relationship to mandated activities.

Conclusion

Our audit found instances of noncompliance with the requirements outlined above. These instances are described in the accompanying Summary of Program Costs (Schedule 1) and in the Findings and Recommendations section of this report.

For the audit period, Santa Clara County claimed $7,396,444 for costs of the Consolidated Handicapped and Disabled Students (HDS), HDS II, and SEDP Program. Our audit found that the entire amount is unallowable.

For the fiscal year (FY) 2006-07 claim, the State paid the county $1,130,322. Our audit found that the claimed costs are unallowable. The State will offset $1,130,322 from other mandated program payments due the county. Alternatively, the county may remit this amount to the State.

For the FY 2007-08 claim, the State paid the county $801,665. Our audit found that the claimed costs are unallowable. The State will offset $801,665 from other mandated program payments due the county. Alternatively, the county may remit this amount to the State.

For the FY 2008-09 claim, the State made no payment to the county. Our audit found that the claimed costs are unallowable.

For the FY 2009-10 claim, the State made no payment to the county. Our audit found that the claimed costs are unallowable.

Views of Responsible Officials

We issued a draft audit report on October 7, 2014. Emily Harrison, Director of Finance, responded by letter dated October 17, 2014 (Attachment), agreeing with the audit results except for Finding 6. The final audit report includes the county's response.

Restricted Use

This report is solely for the information and use of Santa Clara County, the California Department of Finance, and the SCO; it is not intended to be and should not be used by anyone other than these specified parties. This restriction is not intended to limit distribution of this report, which is a matter of public record.

Original signed by

JEFFREY V. BROWNFIELD, CPA
Chief, Division of Audits

October 21, 2014

Schedule 1—
Summary of Program Costs
July 1, 2006, through June 30, 2010

Cost Elements	Actual Costs Claimed	Allowable per Audit	Audit Adjustment	Reference[1]
July 1, 2006, through June 30, 2007				
Direct costs:				
Referral and mental health assessments	$ 3,611,799	$ 3,320,193	$ (291,606)	Findings 1, 2
Participation as member of IEP team	31,447	—	(31,447)	Finding 3
Designation of lead case manager	10,008	—	(10,008)	Findings 1, 3
Psychotherapy/other mental health services	11,012,154	10,230,446	(781,708)	Finding 2
Total direct costs	14,665,408	13,550,639	(1,114,769)	
Indirect costs	1,456,275	989,197	(467,078)	Finding 5
Total direct and indirect costs	16,121,683	14,539,836	(1,581,847)	
Less other reimbursements	(14,991,361)	(15,446,056)	(454,695)	Finding 6
Total claimed amount	1,130,322	(906,220)	(2,036,542)	
Adjustment to eliminate negative balance	—	906,220	906,220	
Total program cost	$ 1,130,322	—	$ (1,130,322)	
Less amount paid by State[2]		(1,130,322)		
Allowable costs claimed in excess of (less than) amount paid		$ (1,130,322)		
July 1, 2007, through June 30, 2008				
Direct costs:				
Referral and mental health assessments	$ 3,047,259	$ 3,139,467	$ 92,208	Finding 2
Authorize/issue payments to providers	3,062,497	2,319,243	(743,254)	Findings 1, 4
Psychotherapy/other mental health services	9,217,936	9,521,869	303,933	Findings 1, 2
Participation in due process hearings	65,772	—	(65,772)	Findings 1, 3
Total direct costs	15,393,464	14,980,579	(412,885)	
Indirect costs	1,343,128	967,326	(375,802)	Finding 5
Total direct and indirect costs	16,736,592	15,947,905	(788,687)	
Less other reimbursements	(15,569,382)	(18,210,730)	(2,641,348)	Finding 6
Total claimed amount	1,167,210	(2,262,825)	(3,430,035)	
Adjustment to eliminate negative balance	—	2,272,825	2,272,825	
Less late claim penalty[3]	—	(10,000)	(10,000)	
Total program cost	$ 1,167,210	—	$ (1,167,210)	
Less amount paid by State[2]		(801,665)		
Allowable costs claimed in excess of (less than) amount paid		$ (801,665)		

Schedule 1 (continued)

Cost Elements	Actual Costs Claimed	Allowable per Audit	Audit Adjustment	Reference[1]
July 1, 2008, through June 30, 2009				
Direct costs:				
Referral and mental health assessments	$ 3,485,007	$ 3,614,580	$ 129,573	Finding 2
Authorize/issue payments to providers	2,836,468	2,166,511	(669,957)	Findings 1, 4
Psychotherapy/other mental health services	8,766,427	9,332,699	566,272	Findings 1, 2
Participation in due process hearings	24,221	—	(24,221)	Findings 1, 3
Total direct costs	15,112,123	15,113,790	1,667	
Indirect costs	913,761	1,113,466	199,705	Finding 5
Total direct and indirect costs	16,025,884	16,227,256	201,372	
Less other reimbursements	(15,911,680)	(17,277,409)	(1,365,729)	Finding 6
Total claimed amount	114,204	(1,050,153)	(1,164,357)	
Adjustment to eliminate negative balance	—	1,050,153	1,050,153	
Total program cost	$ 114,204	—	$ (114,204)	
Less amount paid by State		—		
Allowable costs claimed in excess of (less than) amount paid		$ —		
July 1, 2009, through June 30, 2010				
Direct costs:				
Referral and mental health assessments	$ 2,733,021	$ 3,560,237	$ 827,216	Finding 2
Authorize/issue payments to providers	2,856,260	2,208,184	(648,076)	Findings 1, 4
Psychotherapy/other mental health services	9,685,804	8,548,914	(1,136,890)	Findings 1, 2
Participation in due process hearings	112,253	—	(112,253)	Findings 1, 3
Total direct costs	15,387,338	14,317,335	(1,070,003)	
Indirect costs	1,096,016	1,053,496	(42,520)	Finding 5
Total direct and indirect costs	16,483,354	15,370,831	(1,112,523)	
Less other reimbursements	(11,498,646)	(16,560,522)	(5,061,876)	Finding 6
Total claimed amount	4,984,708	(1,189,691)	(6,174,399)	
Adjustment to eliminate negative balance	—	1,189,691	1,189,691	
Total program cost	$ 4,984,708	—	$ (4,984,708)	
Less amount paid by State		—		
Allowable costs claimed in excess of (less than) amount paid		$ —		

Schedule 1 (continued)

Cost Elements	Actual Costs Claimed	Allowable per Audit	Audit Adjustment
Summary: July 1, 2006 through June 30, 2010			
Direct costs:			
Referral and mental health assessments	$ 12,877,086	$ 13,634,477	$ 757,391
Participation as member of IEP team	31,447	—	(31,447)
Designation of lead case manager	10,008	—	(10,008)
Authorize/issue payments to providers	8,755,225	6,693,938	(2,061,287)
Psychotherapy/other mental health services	38,682,321	37,633,928	(1,048,393)
Participation in due process hearings	202,246	—	(202,246)
Total direct costs	60,558,333	57,962,343	(2,595,990)
Indirect costs	4,809,180	4,123,485	(685,695)
Total direct and indirect costs	65,367,513	62,085,828	(3,281,685)
Less other reimbursements	(57,971,069)	(67,494,717)	(9,523,648)
Total claimed amount	7,396,444	(5,408,889)	(12,805,333)
Adjustment to eliminate negative balance	—	5,418,889	5,418,889
Less late claim penalty[3]	—	(10,000)	(10,000)
Total program cost	$ 7,396,444	—	$ (7,396,444)
Less amount paid by State		(1,931,987)	
Allowable costs claimed in excess of (less than) amount paid		$ (1,931,987)	

[1] See the Findings and Recommendations section.

[2] The county received categorical payments from the California Department of Mental Health from the FY 2009-10 budget.

[3] The county filed its FY 2007-08 annual reimbursement claim after the due date specified in Government Code section 17560. Pursuant to Government Code section 17568, the State assessed a late filing penalty equal to 10% of allowable costs, not to exceed $10,000, for each late claim filed.

Findings and Recommendations

FINDING 1—Misclassification of direct costs

In its claims, the county did not separately report its direct costs for the following three reimbursable components: (1) Designation of Lead Case Manager; (2) Authorize/Issue Payments to Providers; and (3) Participation in Due Process Hearings, as required by the State Controller's Office claiming instructions. The costs of these components were reported by the county in the Referral and Mental Health Assessments and Psychotherapy/Other Mental Health Services components. During the audit, we reclassified the county's direct costs into the appropriate claim components based on information the county provided.

Recommendation

No recommendation is applicable for this report, as the consolidated program no longer is mandated.

County's Response

The county agreed with the finding.

FINDING 2—Overstated assessment and treatment costs

The county overstated assessment and treatment costs by $291,002 for the audit period. Assessment costs were understated by $757,391 and psychotherapy/other mental health services were overstated by $1,048,393. Costs were overstated primarily because the county did not fully support units of services claimed.

The county claimed mental health service costs that were not fully based on actual costs to implement the mandated program. For the audit period, the county provided unit of service reports that represented the finalized units of services rendered to eligible clients. We reviewed the reports and noted that reported units did not reconcile to claimed units. Further, we also noted that the report included ineligible emergency psychiatric services for FY 2006-07.

We recalculated costs based on actual, supportable units of service provided to eligible clients, using the appropriate unit rates that represented the actual costs to the county. We excluded the costs related to emergency psychiatric services for FY 2006-07, which totaled $39,510.

The following table summarizes the adjustments to assessment and treatment costs:

	Amount Claimed	Amount Allowable	Audit Adjustment
FY 2006-07			
Referral and mental health assessments	$ 3,611,799	$ 3,320,193	$ (291,606)
Psychotherapy/other mental health services	11,012,154	10,230,446	(781,708)
Total	$ 14,623,953	$ 13,550,639	$ (1,073,314)
FY 2007-08			
Referral and mental health assessments	$ 3,047,259	$ 3,139,467	$ 92,208
Psychotherapy/other mental health services	9,217,936	9,521,869	303,933
Total	$ 12,265,195	$ 12,661,336	$ 396,141
FY 2008-09			
Referral and mental health assessments	$ 3,485,007	$ 3,614,580	$ 129,573
Psychotherapy/other mental health services	8,766,427	9,332,699	566,272
Total	$ 12,251,434	$ 12,947,279	$ 695,845
FY 2009-10			
Referral and mental health assessments	$ 2,733,021	$ 3,560,237	$ 827,216
Psychotherapy/other mental health services	9,685,804	8,548,914	(1,136,890)
Total	$ 12,418,825	$ 12,109,151	$ (309,674)
Summary 2006-10			
Referral and mental health assessments	$ 12,877,086	$ 13,634,477	$ 757,391
Psychotherapy/other mental health services	38,682,321	37,633,928	(1,048,393)
Total	$ 51,559,407	$ 51,268,405	$ (291,002)

The following table summarizes the calculation of allowable costs:

	Fiscal Year				
	2006-07	2007-08	2008-09	2009-10	Total
County re-run costs	$ 13,590,149	$ 12,661,336	$ 12,947,279	$ 12,109,151	$ 51,307,915
Ineligible emergency psychiatric services	(39,510)	-	-	-	(39,510)
Total amount allowable	$ 13,550,639	$ 12,661,336	$ 12,947,279	$ 12,109,151	$ 51,268,405

The program's parameters and guidelines provide reimbursement for mental health services when required by the pupil's IEP. These services include assessments, collateral, case management, individual and group psychological therapy, medication monitoring, intensive day treatment, and day rehabilitation services. The parameters and guidelines further specify that when providing mental health treatment services, the activities of socialization and vocational services are not reimbursable.

The parameters and guidelines specify that the State will reimburse only actual increased costs incurred to implement the mandated activities, that are supported by source documents that show the validity of such costs.

Recommendation

No recommendation is applicable for this report, as the consolidated program no longer is mandated

County's Response

The county agreed with the finding.

FINDING 3—
Duplicate county costs

The county claimed duplicate salary and benefit costs, and travel costs totaling $243,701. The county claimed $31,447 of costs within the Participation as Member of IEP Team cost component and $10,008 of costs within the Designation of Lead Case Manager cost component. These costs were expensed within the county's direct cost pool. The direct cost pool is used to compute unit rates for various mental health services. Subsequently, these unit rates were used to compute assessment and mental health treatment costs. Allowing the costs would result in duplicate reimbursement.

The county claimed $202,246 of costs within the Participation in Due Process Hearings cost component that were expensed within its indirect cost pool. The indirect cost pool is used to compute indirect cost rates. The rates, in turn, are used to compute and allocate indirect costs. Allowing the costs would result in duplicate reimbursement.

The following table summarizes the adjustments to claimed costs:

	Fiscal Year				
	2006-07	2007-08	2008-09	2009-10	Total
Participation as member of IEP team	$ (31,447)	$ -	$ -	$ -	$ (31,447)
Designation of lead case manager	(10,008)	-	-	-	(10,008)
Participation in due process hearings	-	(65,772)	(24,221)	(112,253)	(202,246)
Total	$ (41,455)	$ (65,772)	$ (24,221)	$ (112,253)	$ (243,701)

The parameters and guidelines specify that the State will reimburse only actual increased costs incurred to implement the mandated activities, that are supported by source documents that show the validity of such costs.

Recommendation

No recommendation is applicable for this report, as the consolidated program no longer is mandated.

County's Response

The county agreed with the finding.

FINDING 4—
Overstated and duplicate residential placement vendor costs

The county overstated residential placement costs, totaling $2,061,287 for the audit period. These costs included board-and-care and mental health treatment costs. Costs were overstated because the county claimed $1,955,889 in mental health treatment "patch" costs that it expensed with its direct or indirect cost pools. For FY 2007-08 and a portion of FY 2008-09, the county expensed the costs within its indirect cost pool, which is used to compute indirect cost rates. In turn, the indirect rates are used to allocate costs and compute indirect costs. For a portion of FY 2008-09 and FY 2009-10, the county expensed the costs within its direct

costs pool, which is used to compute the unit rates. The unit rates are used to allocate direct costs and compute assessment and mental health treatment costs. Allowing these costs would result in duplicate reimbursement.

Additionally, the county claimed $105,398 in board-and-care costs that were incurred outside of the fiscal year of the claim. The county claimed costs based on when the payments were made instead of by the benefit month when the client was placed. In each fiscal year, we moved the costs to the appropriate fiscal year, representing when the costs were incurred.

The following table summarizes the adjustments to residential placement costs:

	Fiscal Year			
	2007-08	2008-09	2009-10	Total
Board-and-care	$ (46,792)	$ (21,132)	$ (37,474)	$ (105,398)
Mental health treatment	(696,462)	(648,825)	(610,602)	(1,955,889)
Total	$ (743,254)	$ (669,957)	$ (648,076)	$ (2,061,287)

The parameters and guidelines specify that the mandate is to reimburse counties for payments to service vendors providing placement of seriously emotionally disturbed pupils in out-of-home residential facilities as specified in Government Code section 7581, and Title 2, *California Code of Regulations*, section 60200.

Government Code section 17560, subdivision (a), specifies that a local agency may file an annual reimbursement claim that details the costs actually incurred for that fiscal year. Further, the parameters and guidelines specify that the State will reimburse only actual increased costs incurred to implement the mandated activities, that are supported by source documents that show the validity of such costs.

Recommendation

No recommendation is applicable for this report, as the consolidated program no longer is mandated.

County's Response

The county agreed with the finding.

FINDING 5—Overstated indirect costs

The county overstated indirect costs by $685,695 for the audit period. Costs were overstated because the county computed its indirect cost rates using preliminary costs and the rates were applied to unsupported direct costs. The county provided recalculated indirect cost rates using finalized amounts from its financial accounting system. The rates were calculated net of offsetting reimbursements related to indirect costs.

We reviewed the recalculated rates and determined that they were reasonable. We recalculated indirect cost rates consistent with the allocations in the county's cost reports. The rates were calculated net of associated revenues and were applied to eligible direct costs in the following cost components: 1) Referral and Mental Health Assessments, and 2) Psychotherapy/Other Mental Health Services.

The following table summarizes the adjustments to indirect costs:

	Fiscal Year				
	2006-07	2007-08	2008-09	2009-10	Total
Allowable direct costs	$ 13,550,639	$ 12,661,336	$ 12,947,279	$ 12,109,151	
Indirect cost rates	7.30%	7.64%	8.60%	8.70%	
Allowable indirect costs	989,197	967,326	1,113,466	1,053,496	4,123,485
Claimed indirect costs	1,456,275	1,343,128	913,761	1,096,016	4,809,180
Audit adjustments	$ (467,078)	$ (375,802)	$ 199,705	$ (42,520)	$ (685,695)

The parameters and guidelines specify that indirect costs incurred in the performance of the mandated activities and adequately documented are reimbursable.

The parameters and guidelines further specify that indirect costs may be claimed to the extent that they have not already been reimbursed by the California Department of Mental Health (CDMH) from categorical funding sources.

Recommendation

No recommendation is applicable for this report, as the consolidated program no longer is mandated.

County's Response

The county agreed with the finding.

FINDING 6—
Understated offsetting reimbursements

The county understated offsetting reimbursements by $9,523,648 for the audit period. The understatement resulted from the county underreporting reimbursements from Short Doyle/Medi-Cal (SD/MC), Early and Periodic Screening, Diagnosis and Treatment (EPSDT), Individuals with Disabilities Education Act (IDEA), and third-party payor revenues, and from omitting Local Revenue Funds (realignment) and Wraparound program revenues.

In regard to EPSDT, the county used preliminary funding percentages to compute offsetting reimbursements. We recomputed the funding percentages using final cost settlement information from the CDMH.

For residential placement costs, the county omitted realignment revenues, despite using these funds for its 60% share of board-and-care costs. The county accounts for its board-and-care costs within a distinct budget unit, to which it applied realignment funds for its 60% share.

The county also did not identify how it applied $3,000,000 in Wraparound program reinvestment funds. The excess Wraparound funds were identified in FY 2009-10 and returned to the county by its vendors. The Wraparound funds can be used to support services provided to participants of the State-mandated cost program, who are at risk of being placed out-of-home. Further, the county's FY 2009-10 claim includes 131 clients who are identified as participating in both the State-mandated cost program and the Wraparound program. The FY 2009-10 gross direct costs related to Wraparound clients included in the county's claim totaled $5,476,064. We requested that the county provide its accounting records to show how Wraparound reinvestment funds were used. The county has not provided this information. Therefore, we are applying the entire amount as offsetting reimbursement for FY 2009-10.

We recalculated allowable offsetting reimbursements for all relevant funding sources and applied the appropriate rates for SD/MC and EPSDT. We applied all relevant revenues to the full extent of the funding provided, including IDEA funds, CDMH categorical funds, and third-party payor revenues. For out-of-home residential placements, we applied the California Department of Social Services (CDSS) 40% share to eligible board-and-care costs. Further, we applied realignment funds to the extent of the county's 60% share of eligible board-and-care costs. Last, we applied the Wraparound reinvestment funds as an offset to FY 2009-10 costs.

The following table summarizes the adjustments to offsetting reimbursements:

	Amount Claimed	Amount Audited	Audit Adjustment
FY 2006-07			
SD/MC	$ (3,035,944)	$ (2,586,154)	$ 449,790
EPSDT	(924,591)	(1,828,928)	(904,337)
IDEA	(5,918,277)	(5,918,277)	-
CDMH categorical	(5,112,549)	(5,112,549)	-
Third-party payors	-	(148)	(148)
Total	$ (14,991,361)	$ (15,446,056)	$ (454,695)
FY 2007-08			
SD/MC	$ (2,408,059)	$ (2,759,864)	$ (351,805)
EPSDT	(1,589,319)	(2,524,216)	(934,897)
IDEA	(5,918,277)	(5,918,277)	-
CDMH categorical	(4,687,648)	(4,687,648)	-
Third-party payors	-	(1,482)	(1,482)
CDSS 40% share	(966,079)	(927,697)	38,382
Realignment	-	(1,391,546)	(1,391,546)
Total	$ (15,569,382)	$ (18,210,730)	$ (2,641,348)

	Amount Claimed	Amount Audited	Audit Adjustment
FY 2008-09			
SD/MC	$ (2,935,586)	$ (2,794,882)	$ 140,704
EPSDT	(1,215,773)	(1,444,969)	(229,196)
IDEA	(5,918,277)	(5,918,277)	-
CDMH categorical	(4,952,323)	(4,952,323)	-
Third-party payors	-	(447)	(447)
CDSS 40% share	(889,721)	(866,604)	23,117
Realignment	-	(1,299,907)	(1,299,907)
Total	$ (15,911,680)	$ (17,277,409)	$ (1,365,729)
FY 2009-10			
SD/MC	$ (3,426,039)	$ (3,406,665)	$ 19,374
EPSDT	(1,190,964)	(1,626,726)	(435,762)
IDEA	(5,918,277)	(6,317,758)	(399,481)
Third-party payors	-	(1,189)	(1,189)
CDSS 40% share	(963,366)	(883,274)	80,092
Realignment	-	(1,324,910)	(1,324,910)
Wraparound	-	(3,000,000)	(3,000,000)
Total	$ (11,498,646)	$ (16,560,522)	$ (5,061,876)
Total			
SD/MC	$ (11,805,628)	$ (11,547,565)	$ 258,063
EPSDT	(4,920,647)	(7,424,839)	(2,504,192)
IDEA	(23,673,108)	(24,072,589)	(399,481)
CDMH categorical	(14,752,520)	(14,752,520)	-
Third-party payors	-	(3,266)	(3,266)
CDSS 40% share	(2,819,166)	(2,677,575)	141,591
Realignment	-	(4,016,363)	(4,016,363)
Wraparound	-	(3,000,000)	(3,000,000)
Total	$ (57,971,069)	$ (67,494,717)	$ (9,523,648)

The parameters and guidelines specify that any direct payments (categorical funds, SD/MC, EPSDT, IDEA, and other reimbursements) received from the State that are specifically allocated to the program, and/or any other reimbursements received as a result of the mandate, must be deducted from the claim.

The parameters and guidelines also provide that Welfare and Institutions Code section 18355.5 applies to this program and prohibits a county from claiming reimbursement for its 60% share of the total residential and non-educational costs of a seriously emotionally disturbed pupil placed in an out-of-home residential facility, if the county claims reimbursement for these costs from the Local Revenue Fund identified in Welfare and Institutions Code section 17600, and receives the funds.

The Wraparound program was established by SB 163, Chapter 795, Statutes of 1997, to provide a variety of services to eligible clients in lieu of out-of-home residential placement. Program participants include children and youth at risk of being placed voluntarily in an out-of-home residential placement pursuant to Government Code section 7572.5.

Recommendation

No recommendation is applicable for this report, as the consolidated program no longer is mandated.

County's Response

In its draft report, the State Controller's Office (SCO) identifies a number of offsetting reimbursements it contends were erroneously understated in the County's claim. Below, we address each source of potential offsetting reimbursement identified in the draft report:

A. Realignment (Local Revenue Fund):

The Draft Report asserts that "[f]or residential placement costs, the count omitted realignment revenues, despite using these funds for its 60% share of board-and-care costs." The County believes the planned disallowance of $4,016,363 based on these Local Revenue Funds (LRF) is an incorrect reduction, and will deny the County more than $4 million in reimbursements to which it is entitled.

For example, in Fiscal Year 2009-10, the County Social Services Agency (SSA) received LRF totaling $47,155,911.00, and an additional $535,622,197.04 in other state and federal revenue and reimbursements. That same year, SSA had $678,574,874.96 in expenditures for all programs, services, and related costs, resulting in a net cost to the County General Fund of $95,796,766.92. The following table identifies the specific budget units into which the LRF were allocated and the relevant expenses were booked. It also identifies the net cost to the County General Fund associated with these expenses.

SSA FY 2010 Fund 0001					
BU	Expenditures	Other Revenue	Reimbursements	1991 Realignment Revenue	Net County General Fund
BU 116	74,406,859.66	31,019,115.90		10,249,549.00	33,138,194.76
BU 501	404,668,563.62	350,298,024.28	309,955.30	32,172,683.00	21,887,901.04
BU 509	6,538,288.51	4,282,773.89		-	2,255,514.62
BU 511	192,961,163.17	149,712,327.67		4,733,679.00	38,515,156.50
TOTAL	678,574,874.96	535,312,241.74	309,955.30	47,155,911.00	95,796,766.92

The County has also provided the SCO with verifiable accounting records establishing that all LRF were expended on legitimate programmatic and related expenses unrelated to the program at issue here, with no receipts omitted or understated, as was indicated in the SCO's Draft Audit Report.

In the Draft Audit Report and during the exit conference, SCO staff identified Welfare and Institutions Code (WIC) section 18355.5 as the basis for this disallowance. SCO staff asserted that this provision of the WIC allows the SCO to review the specific budget unit into which the LRFs and claimed costs were booked without looking at documentation related to the SSA budget as a whole, and to make the four-million-dollar disallowance on the basis of only that very limited review. The County respectfully disagrees with the SCO's position that WIC section 18355.5 supports this approach. The WIC provision states: "Notwithstanding any provision of law, counties shall not claim reimbursement pursuant to Part 7 (commencing with Section 17500) of

Division 4 of title 2 of the Government Code for costs of 24-hour out-of-home care for seriously emotionally disturbed children who are placed in accordance with Section 7572.5 of the Government Code, if those costs are claimed by the county under this chapter *and the county receives reimbursement for those costs through the Local Revenue Fund established pursuant to Section 17600."* (Cal. Welf. & Inst. Code, former§ 18355.5, emphasis added.) Neither this provision of the WIC nor any other statute, regulation, or other source of authority identified by SCO staff either requires or prohibits the use of any specific County budget structure in order to establish, for SB 90 purposes, that the County was not reimbursed for claimed costs by virtue of its receipt of LRF. Instead, the local budget or accounting structure is at the discretion of the County, so long as this structure allows the County to demonstrate that it used County General Fund dollars to cover program expenses.

Santa Clara County's budget structure allows it to demonstrate that it used County General Fund to cover program expenses, as described above. It is also in full compliance with Governmental Accounting Standards Board standards/Generally Accepted Accounting Principles, and completely and accurately captures all LRF receipts, County expenditures, and the resulting net cost to the County General Fund in County Budget Units (BU) 116, 501, 509, and 511.

In disallowing the $4 million in reimbursements, the Draft Audit Report excludes the totality of verifiable County expenditures and revenue in County Budget Units 116, 501, 509, and 511. Instead, it erroneously narrows reportable expenditures and revenue to *only* Budget Unit 511, and thereby creates an inaccurate and understated net County General Fund cost. Because the Draft Audit Report does not reflect all expenditures and revenue, and because the SCO has provided no basis upon which it may look at only a single County budget unit providing only a small piece of the budgetary information establishing the legitimacy of the County's claim, the County respectfully requests that the LRF disallowance be omitted from the SCO's final audit report.

B. Wraparound Reinvestment Funds:

The Draft Audit Report contains a $3,000,000 disallowance for Wraparound program reinvestment funds because "the county did not identify how it applied $3,000,000 in Wraparound program reinvestment funds" that SSA received from its Wraparound providers in Fiscal Year 2009-10.

As we have explained in previous communications and demonstrated through various documents, the Mental Health Department, which provided and paid for the services being disallowed on the basis of the receipt of Wraparound funds, is fiscally independent from SSA. SSA receives and utilizes all Wraparound funding the County obtains from the State, and did not transfer any of these funds to the Mental Health Department. Accordingly, there is no basis to conclude that *any* Wraparound funds were used to offset any of the costs included in the County's SB 90 claim.

Moreover, there is also no basis to suggest that the County *should* have used any of its Wraparound funds to offset the costs included in its SB 90 claim. Indeed, had the County done so, it would have run afoul of the purpose of the Wraparound program and the guidance issued by the State regarding the appropriate use of Wraparound reinvestment funds. For example, in its April 7, 1999 All County Information Notice

providing guidance for counties implementing the Wraparound program, the California Department of Social Services (CDSS) set forth various fiscal standards, including a requirement that counties have "[p]olicies ... in place to ensure that any cost savings realized from utilizing Wraparound are reinvested to fut1her expand or enhance services and resources for children and families." (ACIN No. 1-28-99.) And in its November 25, 2008 All County Information Notice regarding Wraparound, CDSS further clarified that "Counties should remember that Wraparound requires a braided funding strategy. Children in foster care have multiple funding streams that should be accessed to pay for mental health and health care needs. *It is important to continue to utilize and leverage these funding streams for the child and family."* (ACIN No. I-91-08, emphasis added.) If the County had used Wraparound reinvestment funds to offset the expenses included in its SB 90 claim rather than claiming these expenses through the SB 90 process, its actions would have been inconsistent with the State's direction. Instead, the County was directed to "continue utiliz[ing] and leverag[ing] [existing] funding streams" like SB 90. Using Wraparound reinvestment monies to offset *existing* HDS-related expenditures would have been inconsistent with the State's direction to use Wraparound reinvestment funds to *"expand or enhance* the services and resources for children and families" – instead, it would instead simply maintain the status quo.

For the reasons set forth above, we respectfully request that the Controller's Office omit the disallowance related to Wraparound reinvestment funding from its Draft Audit Report.

SCO's Comment

The finding and recommendation remain unchanged.

The county applied realignment revenues to fund its share of claimed board-and-care costs. In its response, the county presents cost and revenue information for the county social services agency and shows the budget units that were allocated realignment funds. The county states that the agency incurred costs in excess of reimbursements and, therefore, it claimed reimbursement for costs that were funded using general fund resources.

We disagree. The county tracked board-and-care costs and associated revenues within a separate budget unit. The county's accounting records show that it used realignment funds to fund its share of board-and-care costs for the audit period. In reference to reviewing costs of other programs or departmental costs, we believe that combining the expenditures and revenues of other unrelated budget units, subunits, or the entire agency is not relevant. The county tracked the direct costs and the associated revenues for out-of-home residential placements within a budget subunit; the revenues of various types of placements include both state and federal funds, each having a different county share. In the specific budget unit used to track the direct cost of mandate-related residential placement costs, the county applied realignment funds for its 60% share of costs.

Concerning Wraparound reinvestment funds, the county identified $3 million in excess revenues that its Wraparound vendors had returned in 2010. The amount was identified in FY 2009-10. During the course of the audit, the county provided us information which shows that the county social services agency and county mental health department jointly fund and oversee mental health treatment programs related to the Wraparound program. The Wraparound program includes a significant number of clients that are in the mandate program and receive services from Wraparound providers. Further, the Wraparound funds can be used to support services provided to children and youth at risk of being placed in an out-of-home residential placement pursuant to Government Code section 7572.5. In order to affirmatively conclude that no reinvestment funds were applied towards these costs, we asked the county to provide its accounting records showing how the returned funds were used. The county did not provide this information. Consequently, we applied the amount of returned funds as an offset towards mandate program costs.

The county offered to meet to identify a means of resolving the finding without filing an incorrect reduction claim. As we were unable to resolve the issue during the audit, we believe the filing of an incorrect reduction claim would be the appropriate action.

Attachment—
County's Response to
Draft Audit Report

County of Santa Clara
Finance Agency

County Government Center
70 West Hedding Street, East Wing 2nd floor
San Jose, California 95110-1705
(408) 299-5205 FAX 287-7629

October 17, 2014

Jim L. Spano, Chief
Mandated Cost Audits Bureau
State Controller's Office
Division of Audits
P.O. Box 942850
Sacramento, CA 94250-5874

Subject: Santa Clara County's Reponse to the Consolidated Handicapped and Disabled Students (HDS), HDS II, and SEDP Program (July 1, 2006 through June 30, 2010) Draft Audit Report

Dear Mr. Spano:

Thank you for the Draft Audit Report received by the County on October 7, 2014 for the Consolidated Handicapped and Disabled Students (HDS), HDS II, and SEDP Program for the period July 1, 2006 through June 30, 2010. Below, the County addresses the key findings in the report with which it disagrees, and contextualizes several findings the County does not contest. The County's responses to each of the draft findings are as follows:

Finding 1: Misclassification of direct costs

The County agrees that certain costs were misclassified, but notes that the misclassifications had no effect on the amount claimed.

Finding 2: Overstated assessment and treatment costs

The County agrees with this finding. Utilization reports prepared by the Santa Clara Valley Health and Hospital System's (SCVHHS) Information Systems Department at the time of the filing of the claim did not always match the utilization reports prepared by the SCVHHS Information Systems Department at the onset of this audit. But overall, the difference in total units of service was a de minimis 0.56%.

Findings 3, 4, and 5: Duplicate county costs; Overstated and duplicate residential placement vendor costs; Overstated indirect costs

The County agrees with these findings. The preparation of the SB90 mandate claims and the annual cost reports by different staff persons caused certain staff and vendor costs to be reported as direct costs in one document while they were included in the indirect cost pool in the other.

Board of Supervisors: Mike Wasserman, Cindy Chavez, Dave Cortese, Ken Yeager, S. Joseph Simitian
County Executive: Jeffrey V. Smith

Finding 6: Understated offsetting reimbursements

In its draft report, the State Controller's Office (SCO) identifies a number of offsetting reimbursements it contends were erroneously understated in the County's claim. Below, we address each source of potential offsetting reimbursement identified in the draft report:

A. Realignment (Local Revenue Fund):

The Draft Report asserts that "[f]or residential placement costs, the count omitted realignment revenues, despite using these funds for its 60% share of board-and-care costs." The County believes the planned disallowance of $4,016,363 based on these Local Revenue Funds (LRF) is an incorrect reduction, and will deny the County more than $4 million in reimbursements to which it is entitled.

For example, in Fiscal Year 2009-10, the County Social Services Agency (SSA) received LRF totaling $47,155,911.00, and an additional $535,622,197.04 in other state and federal revenue and reimbursements. That same year, SSA had $678,574,874.96 in expenditures for all programs, services, and related costs, resulting in a net cost to the County General Fund of $95,796,766.92. The following table identifies the specific budget units into which the LRF were allocated and the relevant expenses were booked. It also identifies the net cost to the County General Fund associated with these expenses.

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The County has also provided the SCO with verifiable accounting records establishing that all LRF were expended on legitimate programmatic and related expenses unrelated to the program at issue here, with no receipts omitted or understated, as was indicated in the SCO's Draft Audit Report.

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pursuant to Section 17600." (Cal. Welf. & Inst. Code, former § 18355.5, emphasis added.) Neither this provision of the WIC nor any other statute, regulation, or other source of authority identified by SCO staff either requires or prohibits the use of any specific County budget structure in order to establish, for SB 90 purposes, that the County was not reimbursed for claimed costs by virtue of its receipt of LRF. Instead, the local budget or accounting structure is at the discretion of the County, so long as this structure allows the County to demonstrate that it used County General Fund dollars to cover program expenses.

Santa Clara County's budget structure allows it to demonstrate that it used County General Fund to cover program expenses, as described above. It is also in full compliance with Governmental Accounting Standards Board standards/Generally Accepted Accounting Principles, and completely and accurately captures all LRF receipts, County expenditures, and the resulting net cost to the County General Fund in County Budget Units (BU) 116, 501, 509, and 511.

In disallowing the $4 million in reimbursements, the Draft Audit Report excludes the totality of verifiable County expenditures and revenue in County Budget Units 116, 501, 509, and 511. Instead, it erroneously narrows reportable expenditures and revenue to *only* Budget Unit 511, and thereby creates an inaccurate and understated net County General Fund cost. Because the Draft Audit Report does not reflect all expenditures and revenue, and because the SCO has provided no basis upon which it may look at only a single County budget unit providing only a small piece of the budgetary information establishing the legitimacy of the County's claim, the County respectfully requests that the LRF disallowance be omitted from the SCO's final audit report.

B. Wraparound Reinvestment Funds:

The Draft Audit Report contains a $3,000,000 disallowance for Wraparound program reinvestment funds because "the county did not identify how it applied $3,000,000 in Wraparound program reinvestment funds" that SSA received from its Wraparound providers in Fiscal Year 2009-10.

As we have explained in previous communications and demonstrated through various documents, the Mental Health Department, which provided and paid for the services being disallowed on the basis of the receipt of Wraparound funds, is fiscally independent from SSA. SSA receives and utilizes all Wraparound funding the County obtains from the State, and did not transfer any of these funds to the Mental Health Department. Accordingly, there is no basis to conclude that *any* Wraparound funds were used to offset any of the costs included in the County's SB 90 claim.

Moreover, there is also no basis to suggest that the County *should* have used any of its Wraparound funds to offset the costs included in its SB 90 claim. Indeed, had the County done so, it would have run afoul of the purpose of the Wraparound program and the guidance issued by the State regarding the appropriate use of Wraparound reinvestment funds. For example, in its April 7, 1999 All County Information Notice providing guidance for counties implementing the Wraparound program, the California Department of Social Services (CDSS) set forth various fiscal standards, including a requirement that counties have "[p]olicies . . . in place to ensure that any cost savings realized from utilizing Wraparound are reinvested to further expand or enhance services and resources for children and families." (ACIN No. I-28-99.) And in its November 25, 2008 All County Information Notice regarding Wraparound, CDSS further clarified that "Counties should remember that Wraparound requires a braided funding strategy. Children in

foster care have multiple funding streams that should be accessed to pay for mental health and health care needs. *It is important to continue to utilize and leverage these funding streams for the child and family.*" (ACIN No. I-91-08, emphasis added.) If the County had used Wraparound reinvestment funds to offset the expenses included in its SB 90 claim rather than claiming these expenses through the SB 90 process, its actions would have been inconsistent with the State's direction. Instead, the County was directed to "continue utiliz[ing] and leverag[ing] [existing] funding streams" like SB 90. Using Wraparound reinvestment monies to offset *existing* HDS-related expenditures would have been inconsistent with the State's direction to use Wraparound reinvestment funds to "*expand or enhance* the services and resources for children and families" – instead, it would instead simply maintain the status quo.

For the reasons set forth above, we respectfully request that the Controller's Office omit the disallowance related to Wraparound reinvestment funding from its Draft Audit Report.

C. Early Periodic Screening, Diagnosis, and Treatment (EPSDT):

The County does not contest the planned disallowance of $2,504,192, but notes that it is not the result of any error on the County's part. The final EPSDT settlements for the fiscal years being claimed were not available at the time of claim submissions; therefore, it was necessary to utilize preliminary estimates rather than final data from the State because the final data was not available at the time the County submitted its SB 90 claim. For example, the State did not provide the County with the EPSDT cost settlement for Fiscal Year 2009-10 until May 8, 2014 – several years after the County was required to submit its SB 90 claim for that fiscal year. The delays in payment for the other fiscal years at issue in this audit were similar.

D. Other adjustments:

The County does not contest the remaining planned adjustments.

For the reasons set forth above, the County respectfully requests that the SCO reconsider and revise Finding 6 in its draft audit report. We believe the erroneous reductions described above provide a valid basis for an Incorrect Reduction Claim, but the County would prefer to avoid the time and effort – for both the County and the SCO – associated with the filing of such a claim. We are happy to meet with you and your staff to discuss these issues further and to identify a means of resolving this audit without the need for the County to file an Incorrect Reduction Claim.

If you need more information or have any questions, please contact Kim Le at 408-299-5251 or kim-anh.le@fin.sccgov.org.

Sincerely,

Margaret Olaiz
Financial and Administrative Services Manager

Emily Harrison
Director of Finance

State Controller's Office
Division of Audits
Post Office Box 942850
Sacramento, CA 94250-5874

http://www.sco.ca.gov

S13-MCC-016