

MONTEREY COUNTY

Audit Report

HANDICAPPED AND DISABLED STUDENTS II PROGRAM

Chapter 1747, Statutes of 1984,
and Chapter 1274, Statutes of 1985

July 1, 2003, through June 30, 2006



JOHN CHIANG
California State Controller

October 2008



JOHN CHIANG
California State Controller

October 17, 2008

The Honorable Fernando Armenta, Chairman
Board of Supervisors
Monterey County
168 West Alisal Street, 2nd Floor
Salinas, CA 93901

Dear Supervisor Armenta:

The State Controller's Office audited the costs claimed by Monterey County for the legislatively mandated Handicapped and Disabled Students II Program (Chapter 1747, Statutes of 1984, and Chapter 1274, Statutes of 1985) for the period of July 1, 2003, through June 30, 2006.

The county claimed \$2,309,140 for the mandated program. Our audit disclosed that \$1,036,401 is allowable and \$1,272,739 is unallowable. The county claimed the unallowable costs primarily because it (1) duplicated costs claimed in the Handicapped and Disabled Students Program, (2) claimed ineligible crisis intervention and out-of-state travel costs, and (3) applied incorrect rates and units of service. The State made no payment to the county. The State will pay allowable costs claimed, totaling \$1,036,401, contingent upon available appropriations.

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

Sincerely,

Original signed by

JEFFREY V. BROWNFIELD
Chief, Division of Audits

JVB/sk:vb

cc: Wayne Clark, Ph.D., Director
Behavioral Health Division
Monterey County
The Honorable Michael J. Miller, Auditor-Controller
Monterey County
Todd Jerue, Program Budget Manager
Corrections and General Government
Department of Finance
Stacey Wofford
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Department of Mental Health
Cynthia Wong, Manager
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Audit Report

Summary

The State Controller's Office (SCO) audited the costs claimed by Monterey County for the legislatively mandated Handicapped and Disabled Students (HDS) II Program (Chapter 1747, Statutes of 1984, and Chapter 1274, Statutes of 1985) for the period of July 1, 2003, through June 30, 2006.

The county claimed \$2,309,140 for the mandated program. Our audit disclosed that \$1,036,401 is allowable and \$1,272,739 is unallowable. The county claimed the unallowable costs primarily because it (1) duplicated cost claimed in the HDS Program, (2) claimed ineligible crisis intervention and out-of-state travel costs, and (3) applied incorrect rates and units of service. The State made no payment to the county. The State will pay allowable costs claimed, totaling \$1,036,401, contingent upon available appropriations.

Background

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 the 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 (CSM) determined that this legislation imposed a state mandate reimbursable under Government Code section 17561.

The program's parameters and guidelines establish the state mandate and define reimbursement criteria. The CSM adopted the parameters and guidelines for the Handicapped and Disabled Students Program on August 22, 1991, and last amended it on August 29, 1996. 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.

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 in 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* [emphasis added] to fund assessments, psychotherapy, and other mental health services . . .” and that the finding by the Legislature is “declaratory of existing law.”

On May 26, 2005, the CSM adopted a Statement of Decision for the HDS II Program that incorporates the above legislation and further identifies medication support as a reimbursable cost effective July 1, 2001. The CSM adopted the parameters and guidelines for this new program on December 9, 2005, and made technical corrections to it on July 21, 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.

On January 1, 2006, CSM amended the parameters and guidelines for the HDS Program, allowing reimbursement for out-of-home residential placements beginning July 1, 2004.

Objective, Scope, and Methodology

We conducted the audit to determine whether costs claimed represent increased costs resulting from the Handicapped and Disabled Students II Program for the period of July 1, 2003, through June 30, 2006.

Our audit scope included, but was not limited to, determining whether costs claimed were supported by appropriate source documents, were not funded by another source, and were not unreasonable and/or excessive.

We conducted this performance audit under the authority of Government Code sections 12410, 17558.5, and 17561. We did not audit the county’s financial statements. We conducted the 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.

Conclusion

Our audit disclosed 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, Monterey County claimed \$2,309,140 for costs of the HDS II Program. Our audit disclosed that \$1,036,401 is allowable and \$1,272,739 is unallowable. The State made no payment to the county. The State will pay allowable costs claimed, contingent upon available appropriations.

**Views of
Responsible
Official**

We issued a draft audit report on June 12, 2008. The Honorable Michael J. Miller, Auditor-Controller, responded by letter dated July 17, 2008 (Attachment), agreeing with the audit results. This final audit report includes the county's response.

Restricted Use

This report is solely for the information and use of Monterey 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
Chief, Division of Audits

October 17, 2008

**Schedule 1—
Summary of Program Costs
July 1, 2004, through June 30, 2006**

Cost Elements	Actual Costs Claimed ¹	Allowable per Audit	Audit Adjustment	Reference ²
<u>July 1, 2004, through June 30, 2005</u>				
Assessment costs:				
Transfers and interim placement costs:				
Out-of-state travel costs	\$ 10,985	\$ —	\$ (10,985)	Finding 1
Out-of-state residential costs	60,000	—	(60,000)	Finding 1
Contractors' costs	79,478	—	(79,478)	Finding 1
Case management costs	597,406	—	(597,406)	Finding 1
Less offsetting revenues:				
State categorical funds	(158,078)	—	158,078	Finding 3
Short-Doyle/Medi-Cal	(175,642)	—	175,642	Finding 3
Total assessment costs	<u>414,149</u>	<u>—</u>	<u>(414,149)</u>	
Treatment costs:				
Psychotherapy or other treatment services	2,929,449	—	(2,929,449)	Finding 1
Less offsetting revenues:				
State categorical funds	(486,771)	—	486,771	Finding 3
Short Doyle/Medi-Cal	(540,857)	—	540,857	Finding 3
IDEA funds	(1,302,806)	—	1,302,806	Finding 3
Other	(269,453)	—	269,453	Finding 3
Indirect costs	529,028	—	(529,028)	Finding 2
Total treatment costs	<u>858,590</u>	<u>—</u>	<u>(858,590)</u>	
Total program costs	<u>\$ 1,272,739</u>	<u>—</u>	<u>\$(1,272,739)</u>	
Less amount paid by the State		<u>—</u>		
Allowable costs claimed in excess of (less than) amount paid		<u>\$ —</u>		
<u>July 1, 2005, through June 30, 2006</u>				
Assessment costs:				
Transfers and interim placement costs:				
Out-of-state travel costs	\$ 8,463	\$ —	\$ (8,463)	Finding 1
Out-of-state residential costs	40,800	—	(40,800)	Finding 1
Contractors' costs	60,910	—	(60,910)	Finding 1
Case management costs	570,008	613,471	43,463	Finding 1
Less offsetting revenues:				
State categorical funds	(165,436)	(160,636)	4,800	Finding 3
Short-Doyle/Medi-Cal	(183,818)	(195,755)	(11,937)	Finding 3
Total assessment costs	<u>330,927</u>	<u>257,080</u>	<u>(73,847)</u>	
Treatment costs:				
Psychotherapy or other treatment services	2,980,898	3,531,952	551,054	Finding 1
Less offsetting revenues:				
State categorical funds	(713,015)	(704,902)	8,113	Finding 3
Short Doyle/Medi-Cal	(792,239)	(859,008)	(66,769)	Finding 3
IDEA funds	(1,302,806)	(1,302,806)	—	Finding 3
Indirect costs	532,636	449,890	(82,746)	Finding 2
Total treatment costs	<u>705,474</u>	<u>1,115,126</u>	<u>409,652</u>	

Schedule 1 (continued)

Cost Elements	Actual Costs Claimed ¹	Allowable per Audit	Audit Adjustment	Reference ²
<u>July 1, 2005, through June 30, 2006 (continued)</u>				
Subtotal	1,036,401	1,372,206	335,805	
Less allowable costs that exceed claimed costs ³	—	(335,805)	(335,805)	
Total program costs	<u>\$ 1,036,401</u>	1,036,401	<u>\$ —</u>	
Less amount paid by the State		—		
Allowable costs claimed in excess of (less than) amount paid		<u>\$ 1,036,401</u>		
<u>Summary: July 1, 2004, through June 30, 2006</u>				
Assessment costs:				
Transfers and interim placement costs:				
Out-of-state travel costs	\$ 19,448	\$ —	\$ (19,448)	
Out-of-state residential costs	100,800	—	(100,800)	
Contractors' costs	140,388	—	(140,388)	
Case management costs	1,167,414	613,471	(553,943)	
Less offsetting revenues:				
State categorical funds	(323,514)	(160,636)	162,878	
Short-Doyle/Medi-Cal	<u>(359,460)</u>	<u>(195,755)</u>	<u>163,705</u>	
Total assessment costs	<u>745,076</u>	<u>257,080</u>	<u>(487,996)</u>	
Treatment costs:				
Psychotherapy or other treatment services	5,910,347	3,531,952	(2,378,395)	
Less offsetting revenues:				
State categorical funds	(1,199,786)	(704,902)	494,884	
Short Doyle/Medi-Cal	(1,333,096)	(859,008)	474,088	
IDEA funds	(2,605,612)	(1,302,806)	1,302,806	
Other	(269,453)	—	269,453	
Indirect costs	<u>1,061,664</u>	<u>449,890</u>	<u>(611,774)</u>	
Total treatment costs	<u>1,564,064</u>	<u>1,115,126</u>	<u>(448,938)</u>	
Subtotal	2,309,140	1,372,206	(936,934)	
Less allowable costs that exceed claimed costs ³	—	(335,805)	(335,805)	
Total program costs	<u>\$ 2,309,140</u>	1,036,401	<u>\$(1,272,739)</u>	
Less amount paid by the State		—		
Allowable costs claimed in excess of (less than) amount paid		<u>\$ 1,036,401</u>		

¹ Monterey County's HDS II program claim was filed using case management and treatment costs net of Medi-Cal and EPSDT offsetting revenues. We revised the presentation of claimed costs to reflect actual costs incurred with the associated offsetting revenues.

² See the Findings and Recommendations section.

³ Government Code section 17561 stipulates that the State will not reimburse any claim more than one year after the filing deadline specified in the SCO's claiming instructions. That deadline has expired for FY 2005-06.

Findings and Recommendations

**FINDING 1—
Overstated
assessment and
treatment costs**

The county has a net overstatement of assessment and treatment costs of \$3,192,974 for the audit period.

For fiscal year (FY) 2004-05, the county duplicated \$3,537,840 of costs (\$597,406 case management costs and \$2,929,449 in treatment costs claimed under HDS Program and \$10,985 claimed under the Seriously Emotionally Disturbed (SED) Pupils: Out-of-State Mental Health Services Program). We moved \$60,000 ineligible out-of-state placement costs to the SED Pupils Program, reclassified \$79,478 of claimed contract services from assessment to treatment, and moved the costs to the HDS Program.

For FY 2005-06, the county claimed the following ineligible services: crisis intervention, out-of-state travel costs, and out-of-state placement costs in the amounts of \$24,788, \$8,463, and \$40,800, respectively. Additionally, the county incorrectly classified \$60,910 of the \$121,365 in contractors’ treatment costs as assessment costs and did not claim the balance of \$60,455. The county understated case management costs of \$454,477 and treatment costs of \$43,463 because it applied rates that were not based on actual costs and used units of service that were different from the accounting records. We recalculated program costs using rates that were supported by the cost report and any contractual agreements between the county and the service providers.

The program’s parameters and guidelines specify that the State will reimburse only actual increased costs incurred to implement the mandated activities and supported by source documents that show the validity of such costs. Additionally, the parameters and guidelines state that the claimant is allowed to claim and be reimbursed only for eligible activities.

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

	Fiscal Year		Total
	2004-05	2005-06	
Assessment costs:			
Transfers and interim placements:			
Ineligible out-of-state travel	\$ (10,985)	\$ (8,463)	\$ (19,448)
Ineligible out-of-state placement	(60,000)	(40,800)	(100,800)
Misclassified in-state contractors	(79,478)	(60,910)	(140,388)
Case management	(597,406)	43,463	(553,943)
Total assessment costs	(747,869)	(66,710)	(814,579)
Treatment costs:			
Incorrect units/rates	—	454,477	454,477
Misclassified in-state contractors	—	60,910	60,910
Omitted in-state contractors	—	60,455	60,455
Ineligible crisis intervention	—	(24,788)	(24,788)
Duplicated costs	(2,929,449)	—	(2,929,449)
Total treatment costs	(2,929,449)	551,054	(2,378,395)
Audit adjustment—under/(over)	\$ (3,677,318)	\$ 454,344	\$ (3,192,974)

Recommendation

We recommend that the county use appropriate rates to compute claimed assessment and treatment costs. Additionally, we recommend that the county claim only eligible services.

County’s Response

The county agreed with the audit finding.

**FINDING 2—
Overstated indirect costs**

The county overstated indirect costs by \$611,774 for the audit period.

For FY 2004-05, the county claimed \$529,028 that was previously claimed under the HDS Program. For FY 2005-06, the county calculated the indirect cost rate using a formula that is not consistent with the program’s parameters and guidelines. We recalculated indirect costs using correct units and costs, and applied an allocation methodology that is consistent with the cost report.

The parameters and guidelines specify that indirect costs are eligible for reimbursement if the claimant uses the procedure provided in the Office of Management and Budget (OMB) Circular A-87. Claimants have the option of using 10% of direct labor, excluding fringe benefits, or preparing an Indirect Cost Rate Proposal (ICRP) if the indirect cost rate claimed exceeds 10%.

The following table summarizes the overstated indirect costs:

	Fiscal Year		Total
	2004-05	2005-06	
Audit adjustment—under/(over)	\$ (529,028)	\$ (82,746)	\$ (611,774)

Recommendation

We recommend that the county apply indirect cost rates that are consistent with the program’s parameters and guidelines.

County’s Response

The county agreed with the audit finding.

**FINDING 3—
Overstated revenues
offsets**

The county overstated revenue offsets by \$2,867,815 for the audit period.

For FY 2004-05, the county used offsetting revenues of \$2,933,608 that it previously applied under the HDS Program. For FY 2005-06, the county used an incorrect rate to calculate the EPSDT reimbursement. We excluded revenue offsets that relate to the unallowable costs discussed in Finding 1.

The parameters and guidelines specify that any direct payments (categorical funds, Short-Doyle/Medi-Cal FFP, and other offsets such as private insurance) received from the State that are specifically allocated to the program—and/or any other reimbursement received as a result of the mandate—must be deducted from the claim.

The following table summarizes the understated revenue offsets:

	Fiscal Year		Total
	2004-05	2005-06	
Assessment revenues:			
State categorical funds	\$ 158,078	\$ 4,800	\$ 162,878
Short-Doyle/Medi-Cal fund	175,642	(11,937)	163,705
Total assessment revenues	333,720	(7,137)	326,583
Treatment revenues:			
State categorical funds	486,771	8,113	494,884
Short-Doyle/Medi-Cal fund	540,857	(66,769)	474,088
IDEA Fund	1,302,806	—	1,302,806
Other	269,454	—	269,454
Total treatment revenues	2,599,888	(58,656)	2,541,232
Audit adjustment—under/(over)	\$ 2,933,608	\$ (65,793)	\$ 2,867,815

Recommendation

We recommend that the county offsets all applicable reimbursements against reimbursable costs incurred for this program.

County’s Response

The county agreed with the audit finding.

**Attachment—
County's Response to
Draft Audit Report**

MONTEREY COUNTY



AUDITOR - CONTROLLER

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MICHAEL J. MILLER, CPA, CISA
AUDITOR-CONTROLLER

ALFRED R. FRIEDRICH, CGFM
ASSISTANT AUDITOR-CONTROLLER

July 17, 2008

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

RE: Audit Findings for the Handicapped and Disabled Students II and Seriously Emotionally Disturbed Pupils Out-Of-State Mental Health Services Programs.

Dear Mr. Spano:

We concur with your audit findings of June 12, 2008 regarding unallowable costs for the Handicapped and Disabled Students II Program (Chapter 12747, Statutes of 1984, and Chapter 1274, Statutes of 1985) and the Seriously Emotionally Disturbed Pupils Out-of-State Mental Health Program (Chapter 654, Statutes of 1996) for the period of July 1, 2003, through June 30, 2006.

We have implemented and updated our internal controls procedures to prevent the recurrence of these incidents. Any questions please feel free to contact Nerahoo Hemraj, Chief Deputy Auditor-Controller at 831-755-5088.

Sincerely,

Michael J. Miller
Auditor-Controller
County of Monterey

**State Controller's Office
Division of Audits
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<http://www.sco.ca.gov>