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Memorandum

Date *for* June Gibbs Brown
From *Michael Mangum*
Inspector General

Subject Office of Inspector General's Partnership Efforts - Texas State Auditor's Office Report on the Department of Protective and Regulatory Services' Administration of Foster Care Contracts (Report NO. 00-040 /Health and Human Services, A-06-00-00046)

To
Olivia A. Golden
Assistant Secretary for
Children and Families

We are transmitting for your information and use, the attached final report on an audit of the Texas Department of Protective and Regulatory Services' (TDPRS) Administration of Foster Care Contracts. This review was conducted by the Texas State Auditor's Office (SAO) with staff assistance from our Office of Inspector General (OIG). The objective of the audit was to evaluate contract administration for the various types of contracts associated with children in foster care.

The SAO's audit was a comprehensive review of the contract administration over foster care contracts. We participated with the SAO on the portion of the audit that reviewed child placing agencies, their homes and residential treatment facilities. As such, we provided technical assistance in designing the SAO's approach to this portion of the audit. In addition, our fieldwork included visiting a sample of child placing agencies, their foster homes, and residential treatment facilities.

The SAO's report credits TDPRS for appropriately focusing resources on investigations, foster care placements and case management of at-risk children. However, the report also identifies serious gaps in the oversight of foster care contractors which could undermine TDPRS' efforts to ensure: (1) the safety of the children in its care, and (2) that contractors provide the expected services and comply with contract requirements. For example, TDPRS' monitoring plan for Fiscal Year 1999 was not completed, as only 3 of the 19 residential contractors identified as high-risk received the on-site programmatic and fiscal monitoring visits required by TDPRS. In addition, several contracting problems identified in previous SAO reports had not been corrected. Such problems include:

- ◆ The foster care rate methodology is based upon a number of untested assumptions.

- ◆ The TDPRS lacks adequate assurance about the accuracy of cost reports submitted by foster care providers.
- ◆ The TDPRS has not implemented policies and procedures to verify that child placing agencies are paying their foster homes the required minimum amount of maintenance payment. This was also a prior OIG finding.

The TDPRS agreed with the SAO's findings and has already begun taking action to correct the weaknesses identified in its administration of foster care contracts.

We performed a desk review of the SAO's audit report to satisfy ourselves that the attached audit report can be relied upon and used by the Administration for Children and Families in meeting its program oversight responsibilities.

As we do with all audit reports developed by nonfederal auditors, we have provided as an attachment, a listing of the coded recommendations for your staff's use in working with the State to resolve findings and recommendations through our stewardship program. Attachment A provides a summary of the recommendations.

We plan to share this report with other States to encourage their participation in our partnership efforts. If you have any questions about this review, please let me know or have your staff contact Joseph Green, Acting Assistant Inspector General for Administrations of Children, Family, and Aging Audits, at (301) 443-9742.

Attachments

ATTACHMENT A
CIN: A-06-00-00046

<u>Recommendation Codes</u>	<u>Page</u>	<u>Amount</u>	<u>Resolution Agency</u>	<u>Recommendations</u>
21291310	5	N/A	HHS/ACF	Make effective contract administration a priority.
21290110	8	N/A	HHS/ACF	Improve oversight of residential foster care contractors.
07491910	22	N/A	HHS/ACF	Develop policies and procedures that comprehensively address contract renewal criteria.
07492610	23	N/A	HHS/ACF	Enhance residential child care contract provisions.
33292210	27	N/A	HHS/ACF	Continue efforts to revise the foster care payment methodology.
21291910	28	N/A	HHS/ACF	Keep working to improve the foster care management system.
21236710	33	N/A	HHS/ACF	Expand best practices to improve overall contract administration of purchase of services contracts.

An Audit Report on

The Department of Protective and Regulatory Services' Administration of Foster Care Contracts



Office of the State Auditor
Lawrence F. Alwin, CPA

August 2000

Report No. 00-040

Key Points of Report

An Audit Report on the Department Protective and Regulatory Services' Administration of Foster Care Contracts

August 2000

Overall Conclusion

The Department of Protective and Regulatory Services (Department) has not provided sufficient oversight of residential foster care contractors, but it is now working to strengthen its supervision of contractors. The Department has appropriately focused its resources on investigations, foster care placements, and case management of at-risk children. However, serious gaps in the oversight of foster care contractors could undermine the Department's efforts to ensure (1) the safety of the children in its care, and (2) that contractors provide the expected services and comply with contract requirements. Currently, a daily average of 7,000 children receive foster care through 273 residential care contracts. These contracts totaled \$154 million in fiscal year 1999. We found that contract administration of purchase of services contracts was more effective than it was for residential contracts.

Key Facts and Findings

- The Department needs to strengthen its procedures for overseeing its residential foster care contracts. Consideration of more relevant information in the risk assessment process, completion of the annual monitoring plan, and improvement of training and technical assistance for Residential Contract Managers would improve contract oversight.
- The Department has begun to address a material weakness in monitoring and other contract administration weaknesses identified by the State Auditor's Office. However, the Contract Administration Division, created to improve the Department's administration of contracts, has not corrected all prior weaknesses.
- It is too soon to tell if the pilot foster care system created by Permanency Achieved through Coordinated Efforts will be more effective than the current one. The goal is to improve foster care outcomes for foster children without costing the State more money. Improved outcomes include shorter lengths of stay in foster care and stability of foster care placements.
- Currently in Texas, a daily average of 12,000 children are in foster care. Around 7,000 of these children are placed in foster care through residential care contracts. (These contracts are with child-placing agencies, residential treatment centers, emergency shelters, and independent foster homes, among others.) The other 5,000 children are placed in foster homes that contract directly with the Department.

Contact

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Office of the State Auditor

Lawrence F. Alwin, CPA

This audit was conducted in accordance with Government Code, Sections 321.0132 and 321.0133.

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Executive Summary

The Department of Protective and Regulatory Services (Department) has not provided sufficient oversight of residential foster care contractors, but it is now working to strengthen its supervision of contractors. The Department has appropriately focused its resources on investigations, foster care placements, and case management of at-risk children. However, serious gaps in the oversight of foster care contractors could undermine the Department's efforts to ensure (1) the safety of the children in its care, and (2) that contractors provide the expected services and comply with contract requirements. Currently, a daily average of 7,000 children receive foster care through 273 residential care contracts. These contracts totaled \$154 million in fiscal year 1999. We found that contract administration of purchase of services contracts was more effective than it was for residential contracts.

Most of the weaknesses we identified were in the contract administration of residential care contracts. These contracts are with foster care providers such as child-placing agencies, residential treatment centers, and independent foster homes that provide 24-hour care either directly or through subcontractors. The Department needs to improve its oversight of these contractors and the policies and procedures that guide the oversight and contract renewal processes. We did not review the foster care payment methodology for the residential contracts because the Department has hired a consultant to review and revise the methodology.

Make Effective Contract Administration a Priority

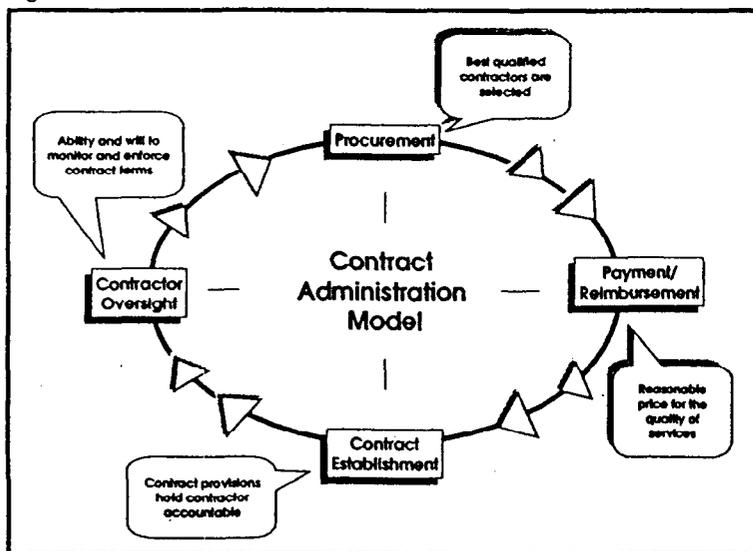
The Department created the Contract Administration Division (CAD) in fiscal year 1996 to improve its administration of contracts. However, some core responsibilities of CAD have not been accomplished. The fiscal year 1999 monitoring plan was not completed, and several contracting problems previously identified by the State Auditor's Office have not been corrected. The Department has not clearly assigned responsibility for cross-functional processes within contract administration. Responsibility for a number of contracting tasks involves various divisions, including Legal, Program, Internal Audit, and regional operations.

Numerous changes in CAD's leadership and staff vacancies may have contributed to weaknesses in contract administration. The Department has begun to address current and prior contract administration problems.

Improve Oversight of Residential Foster Care Contractors

The Department needs to strengthen its procedures for overseeing its residential foster care contracts. Changes that would

Figure 1



or this project, we reviewed the contract administration functions for several types of contracts associated with children in foster care. Contract administration includes four main processes:

- Procurement
- Payment
- Contract establishment
- Contractor oversight

Executive Summary, continued

improve the Department's oversight include the following:

- Consider more risk factors during the risk assessment process to better identify high-risk contractors. More than half of the 10 risk criteria on the risk assessment tool come from the contractors' cost reports, which are self-reported and not audited for accuracy.
- Make completion of the annual monitoring plan a priority. In fiscal year 1999, only 3 of the 19 residential contractors assessed as high-risk received the on-site programmatic and fiscal monitoring visit required by the Department; another 9 received a billing review.
- Document the roles and responsibilities of all staff members involved with residential contracts. Various divisions within the Department share responsibility for many contracting tasks, and responsibility for some of these tasks remains unclear.
- Improve the training and technical assistance that CAD provides to the Residential Contract Managers (RCMs). Many RCMs reported difficulties in getting consistent advice from CAD. Also, CAD has been late in delivering monitoring tools to the RCMs, which delays the start of monitoring activities.

Develop Policies and Procedures That Comprehensively Address Contract Renewal Criteria

Contractor assessments, which provide support for contract renewal decisions, do not consider certain important factors. Inclusion of more detail about the contractor's licensing history, its compliance with contract terms, and meaningful commentary about the contractor's strengths and weaknesses would enable the Department to make more informed renewal decisions.

Enhance Residential Child Care Contract Provisions

The residential contract provisions have improved markedly since 1997. Further enhancements, such as the following, will make the contracts even stronger:

- Provide detail about how the new contract provision that establishes a method of evaluating a contractor's quality of service will be implemented and assessed.
- Clarify Department policy concerning recoupment of unallowable expenditures, and reflect the policy in the contract provisions.
- Describe the Department's rights in property purchased with Department funds and how the rights may be enforced.
- Define related-party transactions, and require contractors to maintain sufficient documentation about these arrangements to ensure the Department of their appropriateness.

Keep Working to Improve the Foster Care Management System

The new foster care model, Permanency Achieved through Coordinated Efforts (PACE), is completing its second year. The Department's goal is to create a more effective system of foster care without increasing the costs of foster care to the State. The pilot project will be evaluated on a set of improved outcomes; however, final results will not be known for a year or more.

Although the legislative requirement to maintain cost neutrality for the pilot project only considers the foster care rate comparison, there are start-up and ongoing administrative costs that are not being tracked.

Executive Summary, concluded

Summary of Management's Responses

The Department has already implemented or is in the process of implementing the recommendations contained in this report. For over a year the Department has made a commitment to resolve issues noted regarding controls over contract administration. These efforts began in June 1999 and evolved into the development of an agency-wide strategic initiative -- Improve Procurement and Monitoring of Purchased Client Goods and Services. This work ultimately resulted in a new organizational structure for the Contract Administration Division (CAD) which was implemented in July 2000. To specifically address issues raised during the course of this audit, a separate Contract Task Force was formed and began work in April 2000 to accelerate progress toward better outcomes. The task force focused on resolving specific audit issues, facilitating efforts already underway and implementing immediate and short-term solutions. This required balancing seasonal contract renewals with the urgent need for improvements in contract monitoring. The task force, which completed work in June 2000, implemented numerous solutions. In addition, a major effort is underway to update and enhance the CAD Handbook.

The Handbook will be an intranet based, user friendly document that will take a contract manager through all the steps of the contracting process. The Handbook is scheduled to be completed and released agency-wide by this fall. The Department believes that the improvements made to date and those scheduled for completion over the next fiscal year will continue to strengthen the contract administration process.

Summary of Objective and Scope

The objective of this project was to evaluate contract administration for the various types of contracts associated with children in foster care. We reviewed contracts for residential care and purchase of services contracts. We also looked at special contracts for (1) the managed care pilot project, (2) an independent evaluator, and (3) revision of the foster care rate setting methodology.

As part of our fieldwork, we visited a sample of child-placing agencies, their foster homes, and residential treatment centers. A team of auditors from the U.S. Department of Health and Human Services, Office of the Inspector General, Office of Audit Services assisted us on these visits.

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Make Effective Contract Administration a Priority

The Department has focused its efforts on direct service delivery and has not made contract administration a priority. As the state agency responsible for protecting at-risk children, the Department has concentrated on investigating allegations of abuse and neglect, placing children in foster care, and tracking their progress. However, more than half of the children in foster care are cared for through residential contracts (see text box), and the administration of these contracts must be a high priority. Good contract administration practices should ensure that contractors meet contract requirements and that foster children receive the required services.

The Department created the Contract Administration Division (CAD) in fiscal year 1996 to improve the Department's administration of contracts. However, the State

Auditor's Office (Office) identified significant weaknesses in the current administration of residential contracts, and several contracting problems identified in prior Office audit reports remain uncorrected.

Types of Residential Child Care Contractors

Child-placing Agencies—organizations that place children in child care facilities, agencies, agency foster homes, agency foster group homes, or adoptive homes, and are licensed by the Department's Child Care Licensing Division.

Residential Treatment Center—facilities that are licensed to provide foster care for 13 or more children at a time.

Emergency Shelter—residential group-care facilities licensed to provide emergency shelter for children.

Agency Foster Home—facilities that provide care for not more than six children for 24 hours a day and are used only by a licensed child-placing agency.

Independent Foster Home—child care facilities licensed to provide care for up to 6 children for 24 hours a day.

Source: Texas Administrative Code and the Department of Protective and Regulatory Services

Numerous changes in CAD's leadership and the departure of experienced staff members have undoubtedly contributed to weaknesses in contract administration. In the four years it has existed, CAD has had four directors and three interim directors. Although CAD is authorized for nine positions, five positions, including the director, were vacant in the spring of 2000. (The remaining four vacancies include two technical assistants, a trainer, and an administrative assistant.)

CAD should ensure that contracts are effectively and consistently administered. Core responsibilities of CAD that have not been accomplished include the following:

- Corrective actions from prior audit reports were not fully implemented. Some problems identified in prior Office audit reports and in a Department audit report remain unresolved. (See Table 1.)
- The fiscal year 1999 monitoring plan was not completed for residential contracts. One of the Residential Contract Managers' (RCMs) responsibilities is to implement CAD's annual monitoring plan. However, CAD does not supervise the RCMs in the regional offices. (The RCMs are supervised by regional management.)

- Guidelines for contracting staff, such as the *Contract Administration Handbook*, monitoring tools, and key policies and procedures, are either out-of-date or non-existent.

Table 1

Uncorrected Problems Identified in Prior Reports	
Date and Source	Finding
SAO Report No. 95-003, September 1994	The foster care rate methodology is based upon a number of untested assumptions. The Department lacks adequate assurance about the accuracy of submitted cost reports.
SAO Report No. 98-041, June 1998 and SAO Report No. 00-555, May 2000	The Department has not implemented policies and procedures to verify that child-placing agencies are paying their foster family homes the required minimum amount.
SAO Report No. 99-555, June 1999 and SAO Report No. 00-555, May 2000	A material weakness exists in the controls over monitoring of vendors with compliance responsibilities for <i>Foster Care - Title IV-E</i> program.
Department Internal Audit Division Contract Administration Audit Report, Audit Number 96-001, August 1997	The risk analysis for residential child care facilities is based on self-reported data from the contractor. Require an independent appraisal (market value analysis) of a related party lease or purchase to ensure the Department pays fair market for related-party transactions.

Source: The State Auditor's Office and the Department of Protective and Regulatory Services

Assign clear responsibility for cross-functional processes within contract administration. Responsibility for numerous contracting tasks is difficult to determine because various divisions, including Legal, Program, Internal Audit, and regional operations share responsibility for many contracting functions. (We noted this problem specifically in relation to residential foster care contracts.)

For example, the Department has not assigned responsibility for implementing a new rule in the Texas Administrative Code (Title 1, Part 15, Section 351.13) that establishes performance measures for the Department's residential contractors. To successfully implement and evaluate these measures, many of the Department's divisions need to work together, and each division needs to understand its role.

RCM responsibilities include the following:

- Enrolling new residential foster care providers
- Renewing residential contracts each year
- Monitoring the residential contractors for contract compliance
- Acting as liaison between the contractors and the Department

The lack of clearly defined responsibility also keeps RCMs from receiving the guidance they need. The RCMs look to CAD, Program, Legal, and Internal Audit for assistance, but they often get little or conflicting information. (See text box for RCM responsibilities.)

As of May 2000, 12 RCMs managed the 273 residential contracts in the State's 11 regions. Contract managers we interviewed were responsible for anywhere from about twenty to sixty residential contracts.

Continue to address contract administration weaknesses. In April 2000, a task force including staff members from all divisions with contracting responsibilities began meeting to develop corrective actions. Another Department task force, created a year ago, is reviewing organizational issues related to contracting agencywide.

Recommendation:

Executive management should clearly assign responsibility for cross-functional processes related to contract administration.

Executive management should continue to closely monitor the progress and implementation of recent Department initiatives that address contract administration weaknesses.

Management's Response:

The Department has already implemented or is in the process of implementing the recommendations contained in this report. For over a year the Department has made a commitment to resolve issues noted regarding controls over contract administration. These efforts began in June 1999 and evolved into the development of an agency-wide strategic initiative -- Improve Procurement and Monitoring of Purchased Client Goods and Services. This initiative is one of six Department-wide initiatives that bring focus to critical agency goals for the current biennium.

The goal of the contracting initiative was to develop and implement procedures for procuring goods and client services and for monitoring contracts to maximize timeliness, flexibility, efficiency and accountability by September 1, 2000. This initiative ultimately resulted in a revised organizational structure for the Contract Administration Division (CAD) which was implemented in July 2000 with the appointment of a new Director of CAD.

To specifically address issues raised during the course of this audit, a separate Contract Task Force was formed and began work on April 1, 2000 to accelerate progress toward better outcomes. The task force focused on resolving specific audit issues, facilitating efforts already underway, and implementing immediate and short-term solutions. This required balancing seasonal contract renewals with the urgent need for improvements in contract monitoring. Improvements identified during the

course of the task force assignment were implemented immediately. These included establishing a contract manager workload standard, updating the fiscal year 2000 monitoring plan, implementing a new risk assessment and modifying monitoring policy for fiscal year 2000 residential contracts, streamlining the renewal process and contract signoff procedures for all contracts, and developing a new risk assessment for fiscal year 2001. The task force completed work on June 30, 2000.

In addition, a major effort is underway to update and enhance the CAD Handbook. The Handbook will be an intranet based, user friendly document that will take a contract manager through all the steps of the contracting process. It will contain samples, job aids, frequently asked questions, and a compendium of legal resources to provide immediate information to contract managers. All sections of the handbook are designed with contract staff input to ensure best practices are incorporated. The first section of the CAD Handbook was completed and tested in July 2000. The Handbook is scheduled to be completed and released agency-wide by this fall.

The Department believes that the improvements made to date and those scheduled for completion over the next fiscal year will continue to strengthen the contract administration process. Department cross-functional processes will be addressed in the Identify Roles and Management Practices for Improved Operations Strategic Initiative. The goal of this initiative is to clarify responsibilities crossing more than one operational area and is scheduled for completion by December 2000. Cross-functional processes regarding client service contracts currently resides in CAD. Regions and state office programs are also responsible for client services contract management. Those contract staff perform tasks including contract negotiation, contract monitoring, contract billing resolution, and contract renewals. Internal Audit will assist Department management in ensuring that the initiatives related to contracts are implemented.

Section 2: OVERSIGHT OF RESIDENTIAL FOSTER CARE CONTRACTS

Improve Oversight of Residential Foster Care Contractors

The Department needs to strengthen oversight procedures for the \$154 million in residential foster care contracts. Changes that would improve the Department's oversight include the following:

- Consider more risk factors during the risk assessment process to better identify high-risk contractors.
- Make completion of the annual monitoring plan a priority.
- Document the roles and responsibilities of all staff members involved with residential contracts.
- Improve the training and technical assistance CAD provides to the RCMs.

Section 2-A: RISK ASSESSMENT

Improve the Risk Assessment Process by Considering Additional Risk Factors

The current risk assessment tools and criteria do not consider all relevant information associated with the residential foster care contractors. As a result, the risk assessment may not identify some high-risk contractors. Problems we noted with the risk assessment tool include the following:

The **risk assessment** for residential child care contracts is a risk analysis of residential contractors that provides the basis for prioritizing and ranking these facilities for contract monitoring purposes. The primary objectives of a risk assessment are to (1) identify, analyze, and act upon risks that might hamper achievement of the Department's objectives, (2) identify risks with higher potential for adverse effects, and (3) determine the priority of risk to be addressed with limited resources.

- More than half of 10 ten criteria on the risk assessment tool come from the contractors' cost reports, which are self-reported and not audited. Also, the emphasis on the cost report figures weights the assessment toward vendors with contracts that have higher dollar amounts; therefore, vendors with contracts of comparatively low dollar amounts are often classified as low risk and never receive on-site monitoring visits. (While large dollar amounts paid to a contractor are certainly a risk factor, numerous other factors also create risk and should be considered.)

- The criterion related to the number of licensing violations received by the contractor does not differentiate between more serious and less serious violations. For example, a torn mattress (a licensing violation) carries the same weight as the absence of a bed for a child.
- The risk assessment tool does not address compliance with contract provisions or quality of care standards.
- The risk assessment tool does not consider the results of prior monitoring visits or the time elapsed since the last monitoring visit.

CAD staff members could not explain changes in the risk rankings of the residential contractors from fiscal year 1999 to 2000. The risk assessment processes for those years were not well documented. The CAD employee responsible for the risk assessment process resigned in December 1999 without documenting the risk analysis for the residential contractors. We reviewed worksheets and other data in an attempt to reconstruct the process and found that:

- Risk rankings were lowered in the absence of additional information. Although most of the fiscal year 1999 contractors rated as high-risk had not received on-site monitoring visits, their risk rankings were lowered for fiscal year 2000. Also, the number of high-risk contractors decreased from 19 to 8 in fiscal year 2000.
- The worksheets appeared to contain inconsistencies and mathematical errors. When we reconstructed some of the fiscal year 2000 risk rankings, the rankings matched the annual plan in only one of five cases.

By clearly documenting and standardizing the risk assessment process, the Department can apply it consistently from year to year.

Recommendation:

The Department should improve the risk assessment tools for the contractors by including factors such as results of monitoring activities, past performance, and compliance with contract provisions. Risk criteria the Department should consider include the following:

- Amount of contractor's growth (revenue, number of children served, number of foster homes)
- Number and/or nature of related-party transactions
- Severity of licensing violations
- Organizational changes (newness, programs added)
- Time elapsed since previous monitoring visit

The Department should also standardize and document the risk assessment process.

Management's Response:

The Contract Task Force developed a new risk assessment tool for all client services contracts that was piloted in three regions and two state office divisions in July 2000. Contract managers completed the tool for fiscal year 2000 contracts and provided feedback regarding the ease or difficulty of using the tool and whether the tool captures risk based on their experience. Results from the pilot have been accumulated and are being analyzed by the Director of CAD.

The piloted tool contains 16 risk factors, including those addressed in the recommendation. The risk assessment tool will be updated and CAD will implement the new risk assessment tool in September 2000 to establish risk and develop the monitoring plan for fiscal year 2001 contracts. The risk assessment process and policy will be documented in the updated CAD Handbook.

Section 2-B: MONITORING COVERAGE

Make Completion of the Annual Monitoring Plan a Priority, and Enhance Monitoring Procedures to Provide Better Oversight of Contractors

Completing the annual monitoring plan is the first of several steps that would improve the monitoring coverage of the Department's residential contractors. Additional procedures include the following:

- Perform financial monitoring of contractors.
- Ensure that the information in CAD's database is complete and accurate.
- Gain more knowledge of foster care providers and share that information with other Department staff members.

In fiscal year 1999, only 3 of 19 residential contractors assessed as high-risk (of 279 total contractors) received the on-site programmatic and fiscal monitoring visit required by the Department's annual contract monitoring plan. Of the remaining 16 high-risk vendors:

- Nine received only a billing review.
- Four did not receive any monitoring.
- Three contracts were terminated after the first six months of fiscal year 1999.

The main purpose of on-site monitoring is to verify that foster children are receiving the required services. Monitoring also provides feedback about foster care contractors for decision-making purposes. A major source of relevant information, feedback about foster care providers enables managers to do meaningful planning related to residential foster care services.

Additionally, the Department plan to sample foster families to verify receipt of the required payments from child-placing agencies was not fully implemented. Residential Contract Managers were to perform this monitoring while conducting site visits, and CAD was to review monitoring reports to ensure completion of the task. Neither process was implemented.

On our visits to a sample of child-placing agencies and foster homes, we identified one child-placing agency that had not paid its foster families the required minimum payments. The child-placing agency deducted computer lease payments from the maintenance payments made to several families for about a year in fiscal year 1998. The deduction of lease payments caused the rate payment to foster families to drop below the minimum amount required.

Conduct financial monitoring of residential contractors. Prior to the spring of fiscal year 2000, there was no substantive financial monitoring of residential contractors. Any financial monitoring done by an RCM was basically a billing review verifying the days of service provided and the level of care payments. The review did

not look at the contractor's expenditures or verify costs reported on the contractor's cost report. Without financial monitoring, the Department lacks assurance that program funds are spent according to contract terms and federal regulations.

In fiscal year 2000, the monitoring tools were changed to include a fiscal monitoring program that looks at accounting and financial records. However, the new financial monitoring tools for fiscal year 2000 were not presented to the RCMs until the end of February.

The Department's Compliance Audit Unit conducts desk reviews (a form of financial monitoring) of the contractors' annual cost reports. However, the Department does not conduct any on-site auditing of the cost reports, which is a violation of the Texas Administrative Code. (See Section 5.)

Ensure that CAD's database contains complete and accurate information. The CAD database that tracks contractor monitoring activities does not contain complete and accurate information. As a result, the database cannot be relied upon as a comprehensive tracking document, and CAD's ability to retrieve meaningful information about contracts from the CAD database by name or type is limited.

CAD and the RCMs did not have the same information about the fiscal year 1999 risk assessment and monitoring plan. High-risk contractors listed in the CAD database for fiscal year 1999 were not always the same as those the RCMs believed to be high-risk. This information is critical to the annual monitoring plan because contractors assessed as high-risk must receive on-site monitoring visits. RCMs rely on accurate and timely information from CAD to complete their annual monitoring requirements.

In addition, we noted the following problems:

- The database contains a number of data entry errors, such as duplication of providers and misidentified regions.
- Eight different abbreviations were used to describe three types of facilities because CAD did not specify a common set of terms to be used.
- CAD could not produce a complete list of the current residential contracts several months after the beginning of fiscal year 2000.
- CAD staff could not provide documentation of approved deviations from the monitoring plan for fiscal year 1999.

An Internal Control Structure Questionnaire (ICSQ) is a tool used by the Department to gather information about a contractor's systems for safeguarding assets, authorizing expenditures, and accurately reporting financial data. An ICSQ requests information about a contractor's record keeping, accounting controls, personnel, travel, equipment, subcontractors, and related-party transactions.

Source: Department of Protective and Regulatory Services

Ensure that all regions use the Internal Control Structure Questionnaires. (See text box.) These questionnaires, one of CAD's monitoring tools, are not being used in some regions. They are required, self-reported assessments to be completed by the contractors. The questionnaires provide the only monitoring coverage for medium- and low-risk contractors. However, no formal guidelines exist; as a result, RCMs may not know how to review these questionnaires, and many contractors receive essentially no monitoring. In one regional office, we found questionnaires in unopened envelopes.

Consider visiting a sample of foster homes when monitoring child-placing agencies. The current monitoring procedures do not include visiting foster homes under the direction of child-placing agencies. Similarly, the Department's Residential Child Care Licensing (Licensing) staff members inspect child-placing agencies for compliance with minimum licensing standards, but these inspectors do not routinely visit foster homes either. Both the contract monitoring process and the licensing regulatory process rely on child-placing agencies to provide assurance that their foster homes are giving appropriate foster care services and complying with licensing standards. This assurance is gained from reading case files on foster children and homes, not from any direct observation. Licensing staff members will visit foster homes to investigate allegations or problem areas identified during child-placing agencies' monitoring visits. The Department plans to request funding for 24 more Licensing positions in the upcoming legislative session. The additional staff members would provide the resources to visit some foster homes as part of their regular inspection process.

Child-placing agencies have primary responsibility for ensuring foster homes' compliance. However, Department staff members cannot verify that child-placing agencies are complying with certain oversight responsibilities without visiting some foster homes themselves. A prior Office report on the Child Care Licensing Division (*Child Care Licensing and Statewide Intake at the Department of Protective and Regulatory Services*, SAO Report No. 98-059, August 1998) identified the need for regulators to visit foster homes on a sample basis. These visits would provide independent verification of child-placing agencies' oversight of foster homes.

Some foster children are not being visited regularly in their foster homes. Managers at several child-placing agencies we visited told us that in a few cases, Department caseworkers were not seeing their assigned foster children as often as guidelines require. A number of foster parents reported that some of their foster children had not seen their Department caseworkers regularly; a few said it had been more than six months since the last caseworker visit. Visits by caseworkers are another means of obtaining information about foster homes.

Enhance information sharing about foster care providers. The Department could improve its oversight by sharing information about foster care. Staff members from different divisions in the Department, each with different objectives, assess various aspects of foster care:

- RCMs enroll new residential foster care contractors, renew the contracts, and monitor the contractors.
- Residential Licensing representatives visit child-placing agencies, residential treatment centers, and independent foster group homes at least annually to inspect for compliance with minimum licensing standards. (Licensing standards place primary responsibility on child-placing agencies for monitoring the foster homes under their direction.)
- Child Protective Services' caseworkers are required to see the foster children on their caseloads once per month and must visit them in their foster homes at least once per quarter.
- Compliance Audit staff members perform desk reviews of contractors' annual cost reports, which contain financial information about their operations.

Opportunities exist for Department staff members to share information about conditions in foster homes and facilities. For example:

- Department staff members use information about a residential contractor's compliance with minimum licensing standards in several ways:
 - RCMs consider compliance with minimum licensing standards when doing the contractor's annual assessment for contract renewal. (See Section 3.)
 - Compliance with licensing standards is a term of the residential contracts.
 - CAD's annual risk assessment of residential contractors uses the number of minimum licensing standards violations as a risk factor.
- Monitoring visits to child-placing agencies by both Licensing staff members and RCMs include following procedures to review files of foster homes and foster children. One purpose of the file reviews is to gain assurance that child-placing agencies are sufficiently overseeing their subcontractors (foster care providers).
- While the caseworker's primary focus when visiting the foster home is the progress of the foster child, the visit also presents the caseworker with the opportunity to observe conditions in the foster home. The caseworker's observations, if shared with Licensing staff members and RCMs, could alert them to potential problems in the foster home.
- When Compliance Audit staff members review contractors' cost reports, they identify expenditures that may warrant further investigation. This information should be given to the RCM to examine on the next monitoring visit.

These types of information sharing occur to some extent in the regional offices, but our discussions with field staff members and foster care providers indicated that improvement and standardization of procedures would benefit most areas.

Ensure that CAD fulfills its role as overseer of residential contract monitoring activities. CAD has failed to provide effective oversight of the residential contract monitoring function. The lack of oversight has contributed to the failure to do the following:

- Ensure progress on the monitoring plan.
- Provide accurate information to executive management regarding the status of the monitoring plan.
- Ensure compliance with contract terms.

CAD made no effort to determine whether Internal Control Structure Questionnaires were received or reviewed by RCMs as required. Also, while CAD did review the monitoring activities of some purchase of services (POS) contract managers on their visits to regional offices, little consideration was given to residential contract monitoring. (See Section 7.)

Recommendation:

The Department should take the necessary steps to improve its monitoring functions for residential foster care providers. These steps should include, but are not limited to, the following:

- Implement oversight procedures for RCMs to ensure that on-site monitoring of high-risk contractors is conducted according to the annual risk assessment and CAD guidelines.
- Improve monitoring procedures to ensure compliance with all significant contract provisions, program requirements, and financial-related requirements. For example:
 - Develop guidelines for a desk review of Internal Control Structure Questionnaires; train the contract managers to identify relevant financial information that can be used in the monitoring process.
 - Sample foster parents to verify receipt of the required payments from child-placing agencies.
- Develop controls to ensure that CAD's tracking database for residential foster care contractors contains accurate, complete, and sufficient information for decision-making and management purposes.
- Develop a standardized report format that can be used to provide CAD and executive management with monthly information about the achievement of the annual monitoring plan and other oversight activities.
- Document approved deviations from the monitoring plan.

- Develop more formalized ways for RCMs, Licensing staff members, and caseworkers to share information about conditions in foster homes. Consider creating a database for this type of information, especially in regions where staff members are not housed in the same office.

CAD should fulfill its role as overseer of residential contract monitoring activities.

Management's Response:

The Department has taken numerous actions to improve monitoring functions for residential contracts. Effective July 1, 2000 the residential contract managers now report centrally to the CPS Program. Residential contract managers are supervised by the Division Administrator for CPS Purchased Services. Specific actions taken to address the recommendation are detailed below.

- *On-site monitoring of high risk contractors has been made a priority by both CPS and CAD. High risk contractors for fiscal year 2000 were identified through the use of a revised risk assessment tool. The Division Administrator for CPS Purchased Services has received from each residential contract manager a schedule that indicates when the monitoring of these high risk contractors will occur. This schedule has been communicated to CAD and is on target for completion by August 31, 2000.*
- *Residential contract managers are performing monitoring procedures to ensure contract compliance. Guidelines for the desk review of Internal Control Structure Questionnaires were provided to all contract managers in June 2000 and use of the guidelines will be included in training conducted by CAD in the fall 2000. A second training class was presented to residential contract managers in May 2000 on the revised financial monitoring tool. In addition, the Division Administrator for CPS Purchased Services has provided on-site monitoring assistance for three residential contracts and has coordinated consultation with CAD. Residential contract managers will continue to sample foster parents to verify receipt of the required payments from child-placing agencies as a part of the financial monitoring and contract compliance tool now being used.*
- *A new procedure, effective May 2000, requires regional and state office program to document deviations from the monitoring plan and submit those deviations to CAD for approval. Deviations for residential contracts are also communicated to the Division Administrator for CPS Purchased Services.*
- *CAD will develop a standardized report format to provide regional and state office management with the information needed to manage contract administration. These reports will include the number of contracts to be monitored by regional and state office program and monthly progress (as reported to CAD) toward goals. These reports will be designed by October 2000 and distributed in November 2000.*
- *Effective June 1, 2000 the updated CAD Handbook instructed contract managers to submit monthly updates to the monitoring plan. CAD staff*

review the monitoring plans and reports submitted and escalate notification of non-compliance to appropriate regional and state office management. CAD Handbook policy will continue to require monitoring plans to be updated to reflect approved deviations. CAD will ensure that the changes are made to the statewide monitoring plan.

- *The Division Administrator for CPS Purchased Services met with Child Care Licensing in June 2000 and began a process to look at how the two divisions could share information more readily with one another. An electronic mailbox where the residential contract managers can get access to licensing non-compliances and inspections with approved passwords is expected to be created by September 1, 2000. The two groups have already agreed to a bi-annual meeting to share ideas and concerns. The current residential monitoring tool requires residential contract managers to contact caseworkers regarding quality services provided by contractors. This practice will be continued with a more formal process to be considered when the contract database is developed.*

Section 2-C: OVERSIGHT ROLES AND RESPONSIBILITIES

Document Roles and Responsibilities for the Oversight of Residential Contracting

As mentioned in Section 1, Department staff members involved in the residential contracting process lack clearly defined roles and responsibilities. As a result, there are gaps in contract oversight. Once executive management assigns responsibility for the different roles, the decisions should be documented, and staff members should be informed.

We noted the following situations:

- RCMs are asked to perform tasks that are no longer in their job description. At one time, RCMs were classified as Institutional Placement Coordinators, and their primary duties were enrolling contractors and providing placement information to caseworkers. In 1997 they became RCMs, and their placement duties were replaced with monitoring responsibilities. However, they were often directed to continue performing child placement functions. In addition, one RCM we interviewed reported that she spent as much as 80 percent of her time managing a large POS post-adoption contract.
- The residential contract renewal process is poorly documented. The lack of clear roles and responsibilities contributed to (1) the late completion of the fiscal year 2000 residential contract re-enrollment, and (2) an incomplete review of fiscal year 2000 re-enrollment contract packages. The late completion of the fiscal year 2000 residential contract re-enrollment resulted in a number of contractors operating without written contracts for short periods of time. The incomplete review of the fiscal year 2000 re-enrollment packages resulted in final contracts that (1) did not contain necessary attachments, (2) did not have supporting documentation related to the contractor, or (3) did not have complete supporting documentation.

- RCMs have trouble getting oversight assistance because it is not clear whom in the Department they should ask. For example, one RCM we interviewed told us that when she takes an issue to CAD, CAD refers her to Program, and Program then refers her to CAD.

Recommendation:

Once executive management clearly defines the roles and responsibilities for contractor oversight, it should clearly document its decisions so that staff members understand them. The documented roles and responsibilities should include, but not be limited to, the following:

- The roles and responsibilities of RCMs should be expressly stated in the *Contract Administration Handbook* or other Department guidelines, and supervisory personnel should ensure that RCMs perform only those duties.
- The *Contract Administration Handbook* should clearly designate who is responsible for the various types of assistance provided to RCMs.
- The Department should strengthen the residential contract renewal process with policies and procedures that include, but are not limited to, a description of the responsibilities of each staff member involved in the renewal process.

Management's Response:

The Contract Administration Division was reorganized effective July 2000. The Division contains three separate areas to ensure that roles and responsibilities for contracting are defined. The first is Legal and Technical Assistance which provides technical assistance to the regions and state office programs, maintains policy and the CAD Handbook, and provides training to Department staff. This section will include two attorneys for legal expertise in contracting. The second area is Quality Assurance which includes updating and maintaining the risk assessment and monitoring tools, maintaining the contract database, and conducting quality assurance reviews of regional and state office contract programs. The third area is cost reporting and fiscal monitoring. In addition to review and on-site auditing of cost reports this area will provide financial technical assistance and recoupment, single audit review, and Permanency Achieved through Coordinated Efforts (PACE) financial monitoring.

The Department will continue to work on documenting roles and responsibilities related to oversight for residential contracts. The roles and responsibilities of the residential contract managers were sent out in a protective services action memo in December 1999. As mentioned in Section 2-B, residential contract managers now report to the Division Administrator for CPS Purchased Services. This will make it easier to respond to any inappropriate responsibilities. CAD and CPS staff will work together to ensure these roles and responsibilities are clearly defined, understood by staff and properly documented.

The contract renewal process was both streamlined and strengthened for fiscal year 2001 contracts. Additional refinement of the process will be developed jointly by CAD and CPS in fiscal year 2001 for implementation with the fiscal year 2002 renewal period.

Section 2-D: TRAINING, MONITORING TOOLS, AND SUPPORT FROM CAD

Improve Contract Administration Division Training and Technical Support to Residential Contract Managers

Develop a sound policy concerning which expenditures should be recouped, and communicate the policy to contractors and Department staff members. The Department does not have a consistent policy regarding recoupment of *unallowable costs* (as defined by federal and state law) incurred by contractors under the unit-rate residential contracts. This inconsistency has resulted in confusion among providers and Department staff members. RCMs cannot properly perform their duties without clear guidance in this area. (The Department has a recoupment policy related to billing errors associated with foster care payments.)

Currently, the residential contract prohibits use of Department funds on unallowable expenditures, and the *Contract Administration Handbook* indicates that such costs are to be recouped by the Department. However, the Department has rarely attempted to recoup these expenditures. For example, we identified a residential foster care contractor who paid a related party \$1,307,559 for administrative services. An undetermined portion of that amount was profit for the related party and may be an unallowable cost. The Department had neither identified nor attempted to recoup this cost. (See definition of related party in Section 4.)

Ensure that CAD provides RCMs with all training necessary to monitor contracts. CAD has not provided RCMs sufficient training to perform all monitoring duties. The role of the RCMs has evolved (see Section 2-C) and has given rise to a need for new skills. Training by CAD has not provided the RCMs with these skills. RCMs reported to us that they did not feel qualified to perform certain financial monitoring duties. For example, training has been deficient in instructing RCMs on the following subjects:

- Evaluating Internal Control Structure Questionnaires intended to assist in contract monitoring efforts
- Evaluating Financial Questionnaires intended to assist in making contract renewal decisions
- Identifying and following through on issues of recoupment of unallowable costs and unapproved property acquisitions
- Ensuring compliance with performance requirements in contracts

Support RCMs with consistent and competent technical assistance from CAD.

- Knowledgeable Staff: RCMs reported to us that they felt CAD staff members were competent in the area of POS contracts but lacked sufficient knowledge about residential contract issues. They also reported that they received different advice depending on which CAD technician they consulted and that it was often difficult to obtain answers. Staff turnover within CAD has undoubtedly contributed to this problem, as staff members with institutional knowledge about residential contract administration have left the Department.
- Timely Monitoring Tools: CAD has been chronically late in delivering monitoring tools to the RCMs. Monitoring tools were not provided to the RCMs until eight months into fiscal year 1999 and five months into fiscal year 2000. This delay postponed the start of monitoring activities, made achievement of the monitoring plan more difficult, and interfered with the time set aside for contract renewal.
- Current Handbook Procedures Related to Monitoring: Parts of the *Contract Administration Handbook* and *Child Protective Services Handbook* are not current and do not reflect current procedures and practices. The *Contract Administration Handbook* has not been updated since 1997. This lack of formal guidance has resulted in confusion among RCMs and inconsistency in the evaluation of providers. Some revisions were made in May 2000, and the revision process is continuing.

RCM staff turnover exacerbates this problem as new staff members try to learn their jobs. Policies make clear that CAD is responsible for developing and maintaining residential contract administration procedures. Areas that need to be addressed or revised include, but are not limited to, the following:

- Applicability of particular sections to POS contracts, residential contracts, or both
- Procedures concerning sanctions for contractor noncompliance, including a framework for applying particular sanctions given different levels of noncompliance
- Monitoring and enforcement of the Department's rights in contractor property purchased with Department funds under unit-rate contracts
- Evaluation of contractor financial information, including the information contained in the Financial Questionnaires received from contractors (which contain useful information regarding the financial condition of the contractor, related-party matters, emerging litigation involving the contractor, and insurance coverage)
- Treatment of related-party transactions
- Coordination of related-party information from different sources (cost report, on-site monitoring tool, Financial Questionnaires, and Internal Control Structure Questionnaires)
- Procedures for recouping unallowable costs

- Procedures for monitoring the amount of maintenance payments passed through to foster parents
- Use of financial monitoring findings in the rate setting process

Recommendation:

The Department should establish a consistent policy concerning recoupment of unallowable costs under unit rate contracts. The policy should be made explicit to both providers and staff members through written guidance that describes when and how recoupment will take place.

The Department should ensure that RCMs receive all training necessary to perform contract monitoring duties including, but not limited to, the following:

- How to evaluate Internal Control Structure Questionnaires intended to assist in contract monitoring efforts
- How to evaluate Financial Questionnaires intended to assist in making contract renewal decisions
- How to identify and follow through on issues of recoupment of unallowable costs and unapproved property acquisitions
- How to ensure compliance with performance requirements in the contract

The Department should support RCMs with consistent and competent technical assistance, including knowledgeable staff, timely monitoring tools, and current handbook procedures related to monitoring.

Management's Response:

The Department will establish a policy regarding recoupment for unit rate contracts. As stated in section 4, the provisions of the contract will be examined and modified for the fiscal year 2002 contract. Handbooks and training for contract managers and for contractors will go into much more detail than the contract, but implementation of actual recoupments will often depend on professional judgments by the Department's attorneys and accountants who have full access to the statutes, regulations and circulars, as do the attorneys and accountants of the contractors. The CAD Handbook will be supplemented by December 31, 2000, and additional training will follow by March 31, 2001.

Residential contract managers will continue to receive training to provide them with the tools needed to perform their job responsibilities. CPS will set residential program policy and will provide guidance on the implementation of overall contracting policy. CAD will establish overall contract policy via the CAD Handbook. CPS and CAD will work together to ensure the policies support each other and are consistent. All items identified by the SAO will be addressed in policy and training during the fall 2000.

CAD will provide support and guidance to regional and state office staff through the new organizational structure described in section 2-C. This assistance will be supported by documented CAD Handbook policy and other means to ensure consistency.

Section 3: RESIDENTIAL CONTRACT RENEWAL

Develop Policies and Procedures That Comprehensively Address Contract Renewal Criteria

We found that while the contractor assessments contain useful information, their quality is inconsistent, and some do not consider certain important factors. (RCMs prepare contractor assessments, which are an important part of the contract renewal decision-making process.) The *Contract Administration Handbook* directs staff to base contract renewal decisions on findings of fact that are appropriately documented. This documentation provides the support for contract renewal decisions. We found that assessments did not consistently:

- Provide sufficient detail of contractors' licensing histories to allow decision-makers to make informed renewal decisions. While contractor assessments often address the contractor's licensing history, it is frequently given only brief mention. This information is most useful if it includes the quantity and nature of licensing violations, disposition or status of those violations, and use of any sanctions or enforcement actions as a result of those violations.
- Address compliance with contract terms. The contractor assessments we reviewed rarely contained any discussion of the contractor's compliance with contract terms or the success with which the contractor was providing services to the children in its care. The 1997 Sunset Advisory Commission Report recommended that the Department "ensure that performance is a factor in any future contract decisions."
- Provide meaningful commentary about contractors' strengths and weaknesses. Contractor assessments that we reviewed rarely presented a useful discussion of the strengths and weaknesses of the contractor. This discussion was either cursory or non-existent.

Recommendation:

The Department should revise contractor assessments to comprehensively address the criteria on which it will base contract renewal decisions. Assessments should do the following:

- Provide sufficient detail of contractors' licensing histories, including the quantity and nature of licensing violations; disposition or status of those violations; and use of any sanctions or enforcement actions as a result of those violations.
- Address contractors' compliance with contract terms.
- Provide meaningful commentary about contractors' strengths and weaknesses.

Management's Response:

The Department has developed a revised residential child care contract assessment outline and instructions. The assessment will provide for greater consistency in contract renewal decision and address the recommendation. Comments are due back on October 1, 2000 for final incorporation and implementation by December 1, 2000.

Section 4: RESIDENTIAL CONTRACT PROVISIONS

Enhance Residential Child Care Contract Provisions

Residential contract provisions have markedly improved since 1997. We believe further enhancements, as outlined below, will make the contracts even stronger.

Revise the new contract provision that establishes a method of evaluating a contractor's quality of service. The fiscal year 2000 Residential Child Care Contracts contain a provision, required by a Health and Human Services Commission regulation (Texas Administrative Code, Rule 351.13), which establishes outcome measures for contractors. This provides a method of assessing a contractor's quality of service. However, the provision lacks sufficient detail and does not explain how the performance measure will be generated or how it will be used to assess contractor performance. Additionally, the wording of the provision creates ambiguity with respect to who has responsibility for monitoring a child's progress under the rule.

The need for useful performance measures has been identified in prior reports. The Office's 1994 Management Control Audit report (*Management Controls at the Texas Department of Protective and Regulatory Services*, SAO Report No. 95-003, September 1994) and the 1997 Sunset Advisory Commission report recommended that Department contracts include clearly defined goals, outputs, and measurable outcomes that directly relate to the program objectives.

Clearly state the Department's rights and the contractor's obligations regarding unallowable costs in accordance with Department policy and state and federal regulations. Contract provisions that addresses unallowable costs are not consistent with Department practices. The Department infrequently attempts to recoup unallowable costs incurred by contractors under unit-rate contracts. As previously mentioned, the Department lacks a clear policy concerning recoupment of unallowable expenditures. (See Section 2-D.) Once established, this policy should be implemented through appropriate regulations and contract provisions. Currently, the contract states that the:

Contractor shall use reimbursements paid by the Department under this contract only to cover allowable costs for services delivered under this contract . . . [t]he LOC [level of care] reimbursement may not exceed the Contractor's actual allowable costs to provide the services under this contract.

If the Department determines that it is both legal and cost-effective to implement a policy of foregoing recoupment of these expenditures, then contract provisions should reflect this determination. On the other hand, if the Department elects to adopt a

policy of pursuing recoupment of these costs, the contract needs to describe the recoupment process.

Describe the Department's rights in property purchased with Department funds and the enforcement of those rights. The current contract does not make clear the Department's rights or the contractor's obligations concerning real or personal property purchased with Department funds. Neither the *Contract Administration Handbook* nor the *Residential Contract Compliance Handbook* provide this guidance. Mere references to federal circulars provide little guidance to either contractors or Department staff members. The *Contract Administration Handbook* directs staff members to take steps to enhance mutual understanding of the contract terms and to take reasonable steps to inform contractors of their responsibilities and liabilities under their contracts.

While it may be impractical for the contract to restate laws and regulations in their entirety due to both their length and complexity, contract provisions should contain enough detail to provide guidance to both parties to the contract. Additionally, the Department should ensure that current terms are legally sufficient to enforce Department rights in such property.

A **related party** is a person or organization related to the residential contractor through common ownership (including an immediate family relationship) or any association that permits either entity to significantly influence or direct the actions or policies of the other. A **related-party** (or "less-than-arms-length") **transaction** is a transaction in which there is an exchange of services, equipment, facilities or supplies between the contractor and the related party.

Address related-party transactions. (See text box.) The contract does not mention related-party transactions. Related-party transactions are commonplace among providers and have been a concern for the Department. While not always inappropriate, these arrangements provide an opportunity for the misuse of Department funds. At a minimum, contract provisions should do the following:

- Define related party.
- Require contractors to maintain documentation sufficient to allow the Department to ensure the appropriateness of these arrangements. This documentation should include support for the cost incurred by the related party in providing the good or service as well as fair market valuations.
- Make specific reference to applicable state regulations and federal circulars that govern related-party transactions.

Specify the type and timing of information to be submitted by the contractor and used by the Department in its subcontract approval process. All contractors are not submitting subcontract information in a timely manner. For example, although the Department requested boilerplate foster home agreements as part of the fiscal year 2000 re-enrollment process, it did not receive copies from all contractors. Ensuring the quality of subcontractors and subcontracts is an important aspect of providing services to children in the Department's care. The current contract requires contractors to obtain Department approval before entering into subcontracts for basic child care services; however, contract provisions do not describe the type and timing of information that must be submitted.

The *Residential Contract Compliance Guide* (RCCG) lists the subcontracting information that contractors should submit to the Department. This information includes boilerplate subcontracts and contractor policies and procedures for monitoring subcontractors. The Department should consider making submission of this information a contract requirement to help ensure that the information is submitted and to provide a basis for RCMs to hold contractors to contract terms.

Additionally, the RCCG states that boilerplate subcontracts that child-placing agencies have with their foster parents must be submitted to the Department. This requirement should be made explicit in the contract.

Require contractors to notify the Department in the event of a change in the contractor's legal name. During the fiscal year 2000 re-enrollment, RCMs encountered contractors who had undergone name changes without informing the Department. The residential child care contract requires the contractor to provide notifications to the Department of any significant change affecting the contractor. However, the contract does not specifically mention a change of corporate name, merger, or dissolution, or provide a specific time frame for notification. Although minimum licensing standards for providers do address such notifications, the problems encountered in this area during the fiscal year 2000 re-enrollment suggest that the contract should specifically address this issue to encourage contractor compliance. By specifically requiring immediate notification of these types of changes and implementing RCM monitoring of this provision, the Department will decrease the likelihood that it will enter into an unenforceable contract with an incorrect or defunct entity.

Recommendation:

The Department should enhance certain Residential Child Care Contract provisions as follows:

- The new contract provision (Paragraph 19(B)(1)) that establishes a method of evaluating a provider's quality of service should be more carefully drafted to provide sufficient detail and explanation concerning how the measure will be generated and how it will be used to assess contractor performance.
- The contract should clearly state the Department's rights and the contractor's obligations regarding unallowable costs and should be consistent with Department policy and state and federal regulations.
- The contract should clearly describe the Department's rights in property purchased with Department funds and how those rights may be enforced.

- The contract should address related-party transactions including, but not limited to, the following:
 - A complete definition of related party.
 - A requirement that contractors maintain documentation sufficient to allow the Department to ensure the appropriateness of any related-party arrangements, including documentation supporting the cost incurred by the related party in providing the good or service and fair market valuations.
 - Specific references to applicable state regulations and federal circulars governing related-party transactions.
- The contract should specify the type and timing of information to be submitted by the contractor and used by the Department in its subcontract approval process.
- The contract should specifically require contractors to notify the Department in the event of a change in the contractor's legal name.

Management's Response:

The Department agrees that provisions of the Residential Child Care Contracts can be updated. Contracts are for the purpose of detailing the special agreements between the parties; they are not for the purpose of detailing every law, regulation and OMB circular. Some parts will be specifically placed in the contract, some statutes and regulations will be specifically cited in the contract, and some parts will be referenced in more general ways in the contract.

Due to the timing of this audit and the Department's contract renewal process, modifications to the contract will be addressed in the fiscal year 2002 contracts. CAD will incorporate the changes more appropriately addressed in the Residential Contract Guide, the CAD Handbook or training during the fall 2000.

- *The provision regarding the providers' quality of service will be clarified in the fiscal year 2002 contract. Because contract language can never be made specific enough to eliminate the need for judgment by the residential contract managers, training will be conducted by CAD to augment contract language in addressing this issue.*
- *The recoupment provisions of the contract will be examined and modified in the fiscal year 2002 contract. Handbooks and training for contract managers and for contractors will go into much more detail than the contract, but implementation of actual recoupments will often depend on professional judgments by the Department's attorneys and accountants who have full access to the statutes, regulations and circulars, as do the attorneys and accountants of the contractors. The CAD Handbook will be supplemented by December 31, 2000, and additional training will follow by March 31, 2001.*

- *Although the current contract is legally adequate because the proper circulars and statutes are cited, the provision regarding rights in property will be made more specific than it is now. Handbooks and training will be enhanced concerning this issue.*
- *The provision regarding related parties will be clarified to address the issues noted. In addition, handbooks and training will also be enhanced. Finally, certain practices by related parties will be considered for inclusion in PRS rules.*
- *For fiscal year 2002 contracts, portions of the Residential Contract Compliance Guide will be incorporated into the contract to address the issue of subcontractor approval.*
- *Notification of name changes will specifically be addressed in the fiscal year 2002 contract.*

Section 5: PAYMENT METHODOLOGY

Continue Efforts to Revise the Foster Care Payment Methodology

The 76th Legislature directed the Department to review, and revise as necessary, the current foster care rate setting methodology. Consequently, the Department has created a work group and hired an outside contractor to assist with this process. Because the consultant's work began during the course of our audit, we did not review the cost methodology.

In SAO Report No. 95-003, *A Review of Management Controls at the Department of Protective and Regulatory Services*, September 1994, we noted that the cost reports on which rates are based had not been audited. This concern remains. The Department has not performed any on-site audits, and thus is in violation of the Texas Administrative Code (TAC). Desk reviews of the contractors' cost reports are now current and provide a level of assurance about the reasonableness of the financial information in the reports. Auditing a sample of cost reports annually would verify the accuracy of the contractors' self-reported financial information. TAC, Section 700.1801(11), requires the Department to perform:

...a sufficient number of on-site audits each year to ensure the fiscal integrity of the 24-hour child-care services program. PRS determines the frequency and nature of on-site audits, and the number of audits performed each year may vary. To maximize the number of audited cost reports available for use in projecting costs, PRS arranges as many on-site audits as possible.

The foster care rate setting methodology uses the financial information in the cost reports as the basis of the foster care rates. Therefore, it is important that the Department audit at least a sample of cost reports annually to determine if the financial information being reported is accurate.

Recommendation:

The Department should audit a sample of cost reports each year to ensure the accuracy of the contractors' cost reports, as required by law.

Management's Response:

Desk review procedures that have been employed provide verification on the accuracy of cost reports, however the Department agrees that on-site review of cost reports would enhance the accuracy of the information. Prior to fiscal year 2000, the Department had a rider provision that specifically prohibited the reduction in foster care rates and did not have funding to increase rates. To resolve a prior audit issue, desk reviews of 1998 cost reports were completed and resulted in over \$8 million in net adjustments. These desk reviews coupled with training of providers on cost reporting enhance the accuracy of the information. Beginning with the 2000 cost reports, which are due from providers beginning December 31, 2000, CAD will supplement the desk review of cost reports with a risk based approach to conducting on-site reviews.

Section 6: PERMANENCY ACHIEVED THROUGH COORDINATED EFFORTS (PACE)

Keep Working to Improve the Foster Care Management System

It is too soon to tell if the pilot foster care system created by Permanency Achieved through Coordinated Efforts (PACE) will be a more effective system than the current one without costing the State more money. The Legislature required the Department to maintain cost neutrality in regard to the pilot project's foster care payments; however, the Department is not tracking the start-up and administrative costs of the pilot project. An independent contractor will be evaluating the effectiveness of the pilot project, using specific outcome measures related to foster care. Final results will not be known for a year or more.

Section 6-A:

Continue Efforts to Evaluate the Foster Care Pilot Project

The nature of the foster care pilot project is to change the existing foster care management system. The Department's goal is to create a more effective system of substitute care without increasing the costs of foster care to the State. Effectiveness of services (improved outcomes) is defined as follows:

- Improved child functioning
- Shortened length of stay in care
- Increased stability of placements within the system of care
- Maintenance of least-restrictive placements

PACE was created in response to Rider 7 during the 75th Legislature, which stated that the Department should consider the "expansion of contract services, regional planning, service outcomes, and appropriate funding mechanisms to be tested in a pilot project . . . and funded at no increased cost to the State." The Department's efforts to maintain cost neutrality do not include start-up costs, cost of administering the program, or any duplication of efforts by field staff members as responsibilities transition to the primary contractor.

Permanency Achieved through Coordinated Efforts (PACE)

The pilot project for substitute care, PACE, is contained in a 10 county area around Fort Worth. The counties include: Cooke, Denton, Erath, Hood, Johnson, Palo Pinto, Parker, Somervell, Tarrant, and Wise. In Phase I of PACE, which began in September 1998 (fiscal year 1999), the primary contractor functions as an umbrella administrative agency for placement, assessment, and treatment of children in foster care. Under Phase II, scheduled to begin sometime in fiscal year 2001, the primary contractor's responsibilities may be expanded.

The target population for PACE includes children with therapeutic needs and children in a sibling group in which at least one sibling has therapeutic needs. In fiscal year 1999, the primary contractor received \$7.7 million to serve a daily average of 291 foster children. In fiscal year 2000, the Department projects that it will pay the primary contractor about \$13.7 million to care for a daily average of 483 foster children.

PACE is completing its second year of Phase I, in which the primary contractor functions as an umbrella administrative agency for placement, assessment, and treatment of children in foster care. The Department plans to expand the project in fiscal year 2001. Phase II is under development, and the scope of services in the second phase has not been determined.

An independent contractor is evaluating PACE on the outcomes defined on the previous page. The initial assessment for fiscal year 1999, the first year of the pilot project, was not completed by May 2000. Moreover, until Phase II is

implemented and sufficient time has elapsed to allow changes in foster care outcomes, the expansion of this foster care model will remain undecided.

Section 6-B:

Devise a System to Capture the Total Costs for Creating and Administering PACE

The Department lacks a system to track how staff members spend their time, and therefore, it cannot capture certain costs related to PACE or other projects. Most costs associated with PACE relate to staff salaries. This cost information is necessary to fully assess the cost-benefit of any current or future innovative pilot projects.

Although the legislative requirement to maintain cost neutrality for the pilot project only considers the foster care rate comparison, there are additional costs associated with PACE:

- Start-up and ongoing administration costs for Department staff in areas such as Program, Accounting, and CAD
- Costs related to duplicative efforts in the field as responsibilities are transferred from Department staff members to the primary contractor

The Legislature did not appropriate additional funds for PACE; the start-up and administrative costs for PACE are funded through current appropriations.

A good time keeping system would allow the Department to further analyze the cost-benefit of PACE, especially once Phase II has been operational for a couple of years. The ability to capture and analyze all costs associated with new programs should be in place before any decisions are made about the implementation of other innovative pilots.

PACE Rates

In fiscal year 1999, the Department paid the PACE primary contractor a daily rate of \$72.40 for each child, regardless of the child's level of care. However, the primary contractor pays its subcontractors a rate that is based on the particular child's level of care.

The daily rate was increased by 7 percent, to \$77.40 per day per child, at the beginning of fiscal year 2000. The 76th Legislature mandated the rate increase for all foster care providers.

The Department is currently paying more, on average, for PACE foster children than for non-PACE children. The daily rate the Department pays the primary contractor for PACE children was determined using payment data from fiscal years 1995-1997. (Using historical data to set the foster care rate is an accepted practice.) However, the population mix of the PACE foster children in fiscal year 1999 differed from the previous years—more children in the pilot project region were placed in foster care than in prior years, and relatively more PACE children required a lower level of care. If the daily rate were calculated on the

actual PACE population in fiscal year 1999, it would have been \$68.24, not \$72.40. The annual overpayment, based on the actual PACE population in fiscal year 1999, was \$440,064.

Recommendation:

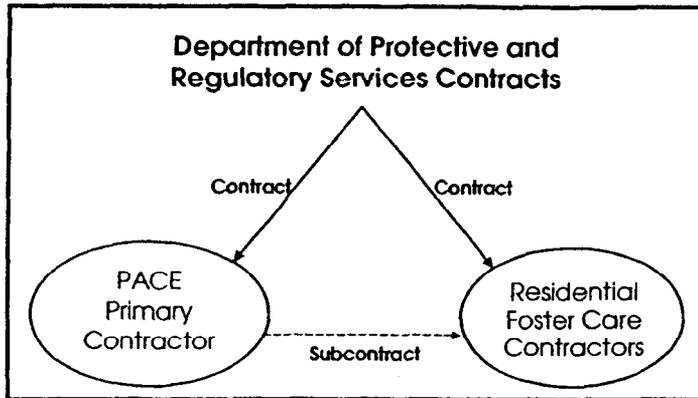
The Department should develop a time keeping system to capture administrative start-up and implementation costs for PACE and other innovative pilot projects to better determine each project's cost benefit.

Management's Response:

We agree that capturing administrative costs would assist in determining a project's cost benefit. The Department ultimately expects to utilize the PeopleSoft Time and Labor module as an enterprise-wide solution to tracking time for all employees. However, this would first require the implementation of the PeopleSoft Human Resource module to run. Due to resource limitations and agency automation priorities, we do not anticipate implementing these PeopleSoft modules until the fiscal year 2004-2005 biennium. In the interim, the Department will review potential solutions for staff working on pilot projects such as PACE and develop an implementation plan by March 1, 2001.

Ensure That the Primary Contractor Sufficiently Monitors Its Subcontractors

Figure 2



On monitoring visits in June and December 1999, Department monitors found weaknesses in the primary contractor's oversight of its 60 subcontractors. Contract provisions require the primary contractor to monitor its subcontractors to ensure that they have the qualifications and financial resources to provide foster care services. The contract also requires the primary contractor to ensure that its subcontractors use foster care funds appropriately.

The primary contractor has 55

subcontractors who also have contracts with the Department. (See Figure 2.) Both the primary contractor and the RCMs are responsible for monitoring these contractors (subcontractors). During fiscal year 1999 and the first half of fiscal year 2000, neither the primary contractor nor the RCMs met all monitoring guidelines for the contractors (subcontractors).

The primary contractor has monitored to determine if foster parents received the minimum amount of maintenance foster care payments required by the Department. The primary contractor conducted spot checks of its subcontractors' foster homes (by telephone) to ask foster parents about the payments they had received.

Recommendation:

The Department should ensure, through regular monitoring of the primary contractor, that it is sufficiently monitoring its subcontractors.

Management's Response:

The programmatic monitoring functions of the PACE contract have now been put under the Division Administrator for CPS Purchased Services. A PACE contract manager position has been authorized. The position is expected to be filled by September 15, 2000. This person will be responsible for ensuring the primary contractor is complying with the subcontractor monitoring requirements in the contract.

Section 6-D:

Continue to Define New Roles and Responsibilities as Additional Phases of PACE Are Implemented

The changing roles associated with PACE initially caused confusion for Department and primary contractor staff members involved in the transfer of responsibilities. PACE was implemented in September 1998, shortly after the contract was awarded, and before the new roles and responsibilities of both parties had been formalized. The primary contractor quickly hired additional staff members to accommodate new responsibilities such as placement, assessment, and case management that were previously performed by Department staff members. Department caseworkers saw their roles change to those of case managers, with the primary contractor assuming more direct care responsibilities for PACE foster children.

We noted a strong commitment to PACE's success on the parts of the Department and the primary contractor when we visited the pilot project region, despite the recent role changes. Noting the need to delineate each party's roles, responsibilities, and job tasks, the Department has wisely delayed the implementation of Phase II of the pilot project until further joint planning can occur.

The Department needs to develop staff members to have specific knowledge of PACE to promote the success of the pilot project. A number of staff members with PACE duties, both in the state office and the regional office, have left the Department since December 1999. CAD's PACE Contract Manager resigned in December 1999 and had not been replaced as of May 2000. Several regional staff members with PACE knowledge and responsibilities, including the RCM and the PACE Liaison Program Director, left in February 2000. CAD's PACE Contract Manager and the RCM had been monitoring the primary contractor semi-annually. As a result of their resignations, the December 1999 monitoring report has not been issued, and expertise about the pilot project was lost. Local expertise with the unique demands of PACE is critical to the pilot project's success, especially as the scope expands under Phase II.

Recommendation:

Before additional responsibilities are transferred to the primary contractor under Phase II, the Department should clearly define, formalize, and communicate new roles, responsibilities, and procedures for case management and program administration.

To the extent possible, the Department should assign responsibilities for PACE to specific staff members in the state office and the regional office, in an effort to develop and increase knowledge of PACE.

Management's Response:

Much effort has been devoted during the past several months to address the issues related to this recommendation in Phase II. Turnover of Department staff dealing with this contract has stabilized and Department executive staff have met to discuss

PACE and specifically outline roles and responsibilities in state office and the region. This has resulted in the creation of a PACE executive committee to facilitate communication and decision making. Designated staff have been provided to improve case management and program administration of PACE. These include a fiscal contract monitor, a program contract monitor, a contract manager, and a budget analyst. The state office person responsible for developing Phase II has transferred to the region to oversee project implementation.

Section 7: PURCHASE OF SERVICES CONTRACTS

Expand Best Practices to All Regions to Improve Overall Contract Administration of Purchase of Services Contracts

Purchase of service contracts are competitively procured contracts for services often provided directly to foster children. The services include evaluation and treatment, which are basic needs assessment and therapeutic services. In fiscal year 1999, the Department spent about \$41 million on services for foster children.

We found that contract administration of POS contracts was more effective than it was for residential contracts. While we identified some aspects of contract administration that could be improved, we also found some best practices in these areas. Efforts that would improve contract administration of POS contracts include the following:

- Standardizing the rate setting process statewide.
- Systematically documenting the negotiation processes.

- Adding programmatic factors and feedback to the risk assessment tool.
- Adding program feedback to the renewal process. Program feedback would also benefit the referral process. (The foster child's caseworker refers the child to the contractor for services.)

In our visits to a number of regional offices, we identified some best practices that would benefit POS contracting in all regions:

- Two regions have implemented market surveys to gather data on rates charged for various contracted services. The surveys give the POS Contract Managers an estimate of where to set rates for therapeutic services.
- One region records issues raised by proposal evaluators on a tracking document. The document is used as a basis for negotiating with prospective contractors.
- One region maintains a program database for feedback about POS contractors. Caseworkers provide input, including complaints about and observations of preferences of the POS contractors. POS Contract Managers review this feedback before awarding new contracts to providers.

POS Contract Managers had conducted financial monitoring of high-risk contractors in the regions we visited. Our testing found that they were following monitoring procedures and documenting their results.

Recommendation:

The Department should expand its best practices statewide to improve contract administration of POS contracts. It should implement processes to do the following:

- Standardize the way rates are set statewide. Collect data within each region so that contract rates reflect local market rates.
- Systematically document the negotiation processes to provide support for contracting decisions.
- Add programmatic factors and feedback to the risk assessment tool so that the risk assessment process considers more relevant information.
- Add programmatic feedback to the contract renewal process so that contractor performance is considered in the renewal process.

Management's Response:

Changes have already been made to the risk assessment tool as discussed in section 2-A. Annual Quality Assurance visits will assess regional and state office contract section's strengths and areas for development as well as compliance with PRS policies. These reports will be analyzed and integrated into an annual summary of best practices and trends in development. The aggregated report will be used in training, the CAD Handbook and job aid tools. In addition, CAD will evaluate all the best practices listed in the recommendation and will implement as appropriate.

Objective, Scope, and Methodology

Objective

The primary objective of this project was to evaluate contract administration for the various types of contracts associated with children in foster care.

Contract administration includes four key areas:

- Procurement—the fair and objective selection of the most qualified contractors
- Payment—the establishment of prices that are cost effective and aligned with the cost of providing the services
- Contract establishment—the inclusion of sufficient provisions to hold the contractor accountable
- Contractor oversight—the monitoring activities and enforcement of the contract terms

Effective contract administration is crucial to the State's ability to ensure that it receives quality services at the best price and that all state and federal requirements are met.

Scope

The scope of this audit included the review of contract administration functions for several types of contracts:

- Contracts for maintenance
 - Residential contracts between the Department and residential child care providers
 - Agreements between the Department and foster care providers
- Purchased services for children in foster care (primarily evaluation and treatment services)
- Special contracts
 - Permanency Achieved through Coordinated Efforts (PACE), a managed care pilot project
 - Youth for Tomorrow, an independent evaluator
 - Consulting contract to revise the foster care rate setting methodology

Methodology

Information collected:

- Interviews with Department executive management and staff members
- Interviews with staff members of foster care contractors
- Interviews with foster care providers, including foster parents
- Interviews with legislative staff members
- Documentary evidence such as:
 - Residential foster care contracts, contract amendments, and extensions
 - Purchase of services (POS) contracts
 - Special contracts (PACE, Youth for Tomorrow, rate setting methodology consultant)
 - Residential contractor assessments
 - Risk assessment tools and documentation for residential and POS contracts
 - Monitoring tools and working papers for all types of contracts
 - Foster care expenditure data
 - Residential contractors' cost reports and Financial Questionnaires
 - Residential contractors' files on foster children and foster homes
 - Residential contractors' financial information
 - The Department's *Contract Administration Handbook*, *Child Protective Services Handbook*, and *Residential Contract Compliance Guide*
 - Minimum licensing standards and guidelines for child-placing agencies, residential treatment centers, and foster homes
 - Relevant parts of the Texas Administrative Code
 - Contract Administration Division Memoranda

Procedures and tests conducted:

- Test of the desk review process for residential contractors' cost reports
- Test of the contract renewal process for residential contracts
- Review of selected financial information at a sample of child-placing agencies and residential treatment centers

- Tests of a sample of child-placing agencies' foster children's files and foster parents' files
- Visits to a sample of foster homes

Criteria used:

- Office Contract Administration Model
- Texas Statutes and Administrative Code
- General Appropriations Act, 75th and 76th Legislatures
- Office of Management and Budget Circulars

Other Information

Fieldwork was conducted from December 1999 through April 2000. The audit was conducted in accordance with *Government Auditing Standards*.

The audit work was performed by the following team members of the State Auditor's staff:

- Babette Laibovitz, MPA (Project Manager)
- Adriana Buford, CPA
- Homer Garcia III, MBA
- Ruby Elizabeth Garcia, CIA
- Dave Gerber, MBA
- Vivek Katyal, MBA
- Walton Persons, CPA
- Henry Siller
- Michael Stiernberg, JD
- Whitney Hutson-Kutz, CPA (Quality Control Reviewer)
- Julie Ivie, CIA (Audit Manager)
- Deborah L. Kerr, Ph.D (Audit Director)

The following team members from the U.S. Department of Health and Human Services, Office of the Inspector General, Office of Audit Services assisted the Office's project team on visits to selected residential contractors and foster homes:

- Sylvie Witten, CPA (Senior Auditor)
- John Raymond, CPA
- Michael Helmick, CPA

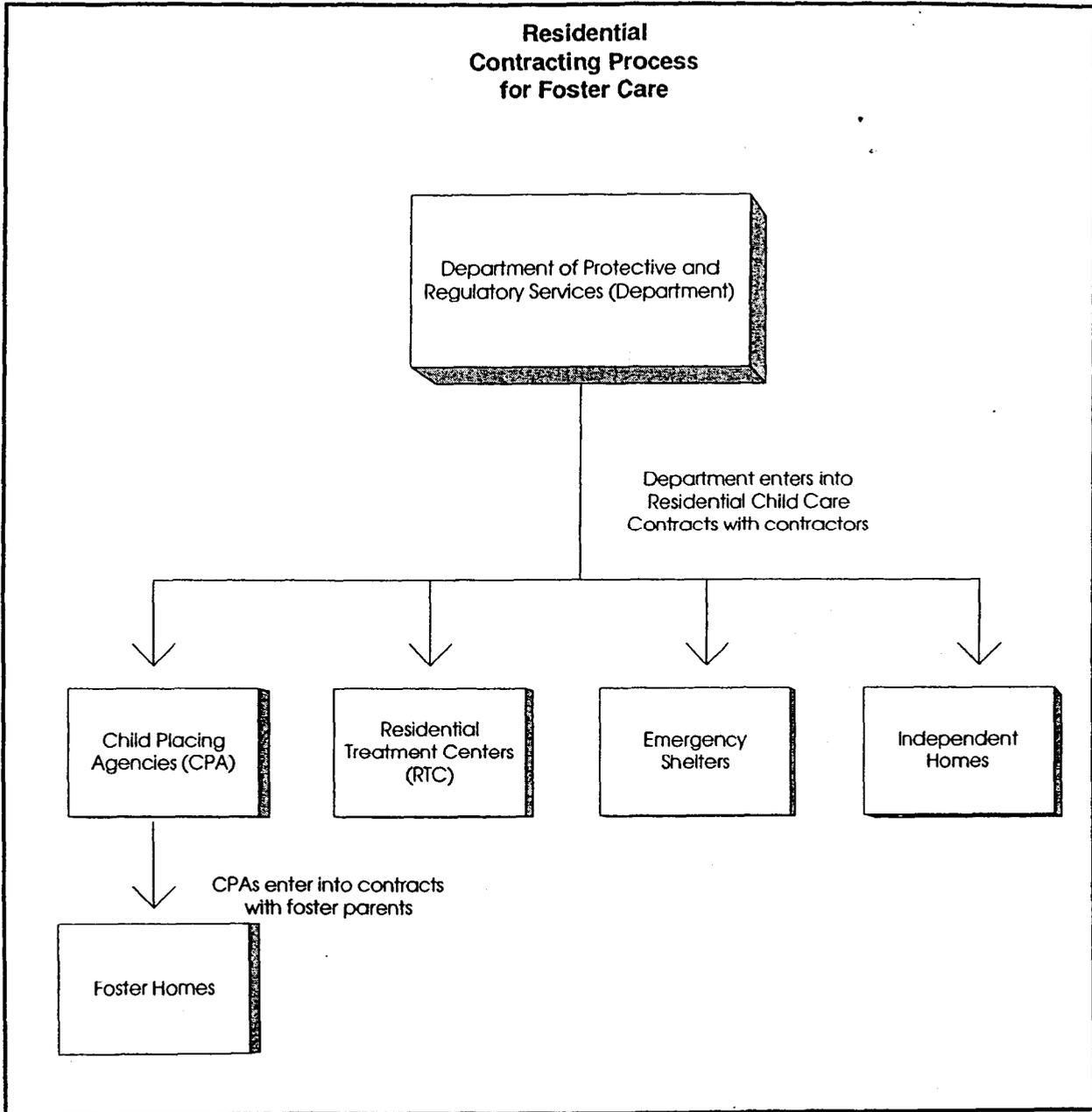
Appendix 2:

Data by Facility Type

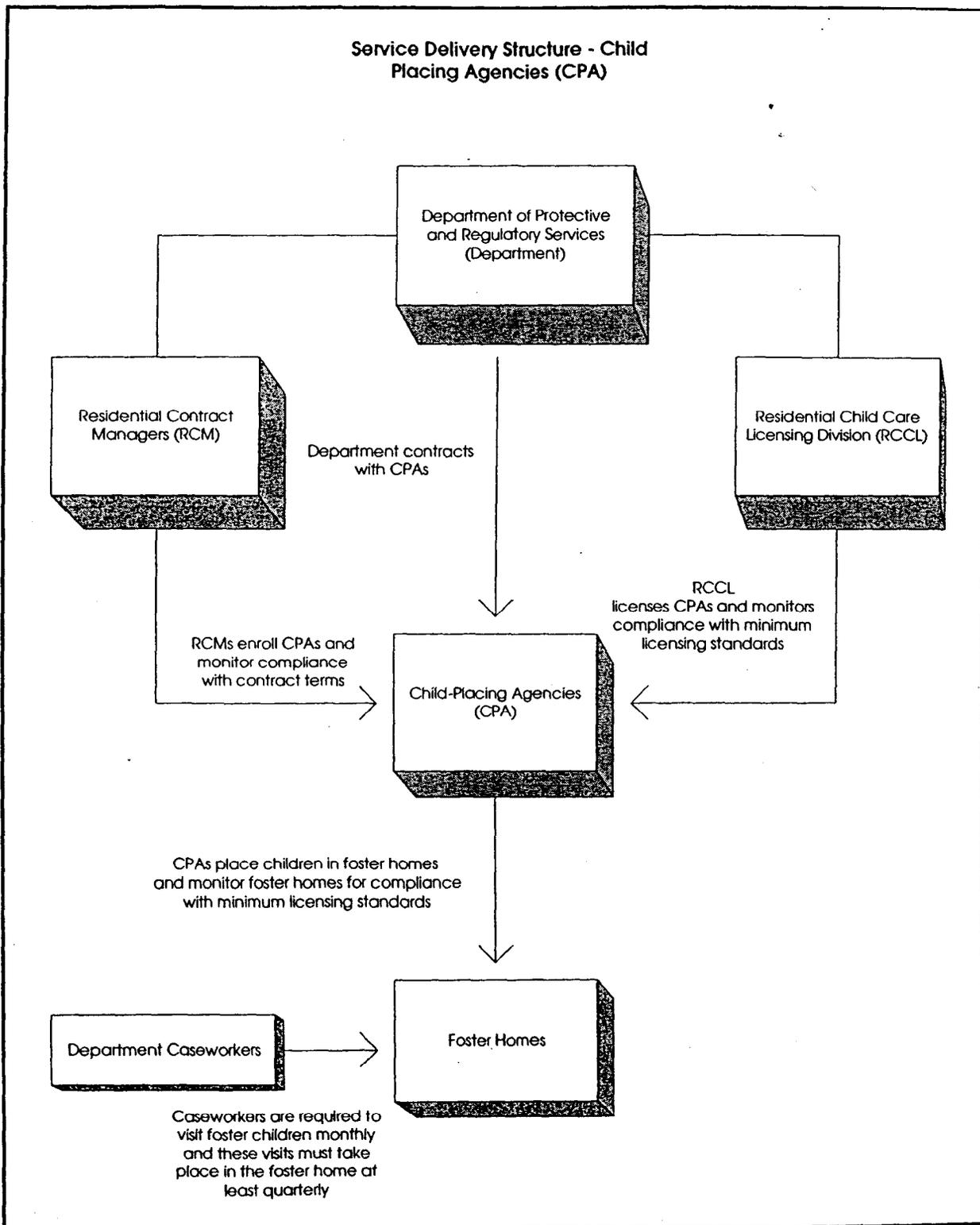
Table 2

Number of Foster Children and Dollars Spent by Facility Type for Fiscal Year 1999				
Facility Group Type	Average Number of Children per Day	Percent of Total Foster Children	Total Dollars Paid for Fiscal Year 1999	Percent of Total Dollars
Child-placing-Agency	3,604	32%	\$ 71,634,614	38%
Residential Treatment Center	1,271	11%	45,131,093	24%
Department of Protective and Regulatory Services Foster Homes ^a	4,938	44%	33,118,238	18%
Independent Homes ^b	568	5%	9,774,242	5%
Emergency Shelter	595	5%	19,548,822	10%
PACE	291	3%	7,699,668	4%
Other	13	0%	227,678	0%
TOTAL	11,280		\$ 187,134,355	
<p>^a Department of Protective and Regulatory Services Foster Homes are foster homes verified by Child Protective Services (CPS) and receive child placements directly from CPS in its capacity as a child-placing agency.</p> <p>^b Independent Homes are composed of basic care facilities, specialized family homes, and specialized group homes.</p>				
Source: Department of Protective and Regulatory Services				

Residential Contracting Process for Foster Care



Service Delivery Structure—Child-Placing Agencies

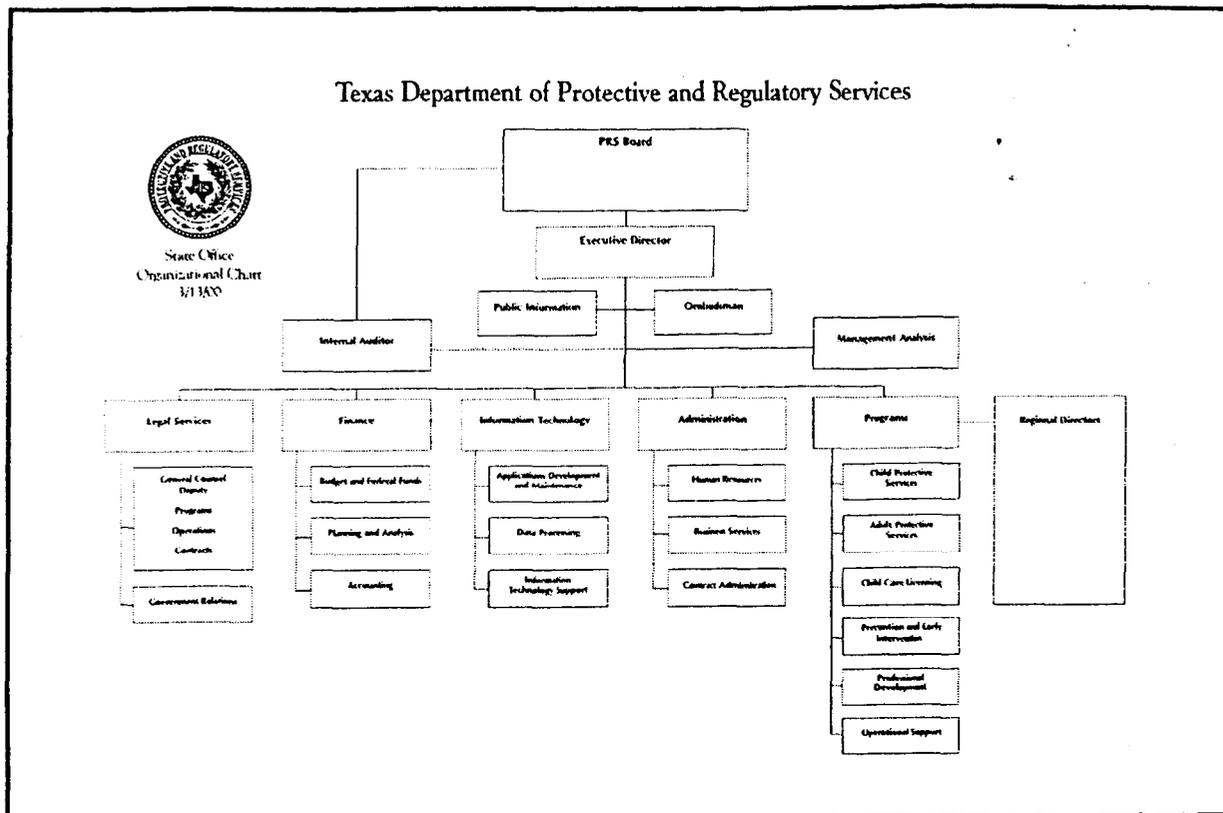


Foster Care Levels of Care

Table 3

Foster Care Levels of Care Rates and Definitions (Fiscal Year 2000)		
Level of Care	Daily Rate	<u>Definition</u> (Texas Administrative Code, Title 40, Part 19, Chapter 700, Subchapter W)
1	\$16.96	Child's functioning is adequate in all developmental and social areas. The child may have transient difficulties and everyday worries and may occasionally misbehave, but he is nonetheless a normal child who responds to normal discipline.
2	\$36.33	Child has problems functioning in one or more areas, but the problems are only occasional. The child sometimes acts out in response to stress, but the episodes of acting out are brief and transient. The child's behavior is minimally disturbing to others and is not considered aberrant by those who know him.
3	\$62.15	Child has frequent or repetitive minor problems in one or more areas of functioning. The child may engage in nonviolent antisocial acts but is able to have meaningful social relationships.
4	\$88.42	Child has substantial problems. The child's physical, mental, or social needs and behaviors may present a low-to-moderate risk of harm to the child or to others. The child may have poor social skills or frequent episodes of aggressive or antisocial behavior. Despite these problems, the child is still able to have meaningful social relationships.
5	\$106.66	Child has severe problems and is unable to function in several areas. The child may lack the motivation or ability to care for himself or participate in social activities, though he may sometimes cooperate when prompted or instructed. The child's reality testing and communications may be severely impaired. The child may exhibit persistent or unpredictable aggression, may be markedly withdrawn and isolated, or may have attempted suicide. The child's behavior may present a moderate-to-severe risk of harm to himself or to others.
6	\$200.98	Child has one or more very severe impairments, disabilities, or needs, and is consistently unable or unwilling to cooperate in his own care. The child may be extremely aggressive or self-destructive. The child's reality testing, communication, cognition, affect, and personal hygiene may be grossly impaired. The child's behavior may present a severe-to-critical risk of serious harm to himself or to others.
Source: Department of Protective and Regulatory Services and Texas Administrative Code		

Appendix 6:
Organizational Chart



Source: Department of Protective and Regulatory Services

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