

**U. S. Department of Agriculture**  
**Office of Inspector General**  
**Audit Report**

**Food and Nutrition Service**  
**Child and Adult Care Food Program**  
**National Report on Program Abuses**

**PRESIDENTIAL INITIATIVE:**  
**OPERATION KIDDIE CARE**

**Audit Report No.**  
**27601-7-SF**  
**August 1999**





UNITED STATES DEPARTMENT OF AGRICULTURE  
OFFICE OF INSPECTOR GENERAL  
Washington D.C. 20250



DATE: August 23, 1999

REPLY TO  
ATTN OF: 27601-7-SF

SUBJECT: Child and Adult Care Food Program (CACFP)  
Operation Kiddie Care

TO: Samuel Chambers, Jr.  
Administrator  
Food and Nutrition Service

This report presents the results of our nationwide review of the CACFP (Operation Kiddie Care) through February 1999. Your written response to the official draft report is included as exhibit E. Excerpts from your response and our position are set forth at the end of each Finding section of the report.

The CACFP is a valuable program for children in child care, but, as shown by the results of Operation Kiddie Care, the CACFP is highly vulnerable to abuse because the primary controls for combatting fraud and abuse have been vested in the CACFP sponsors. We found that some sponsors were using program funds for their personal enrichment and thereby reducing the funds available to provide an effective food service program to children in day care.

While we recognize and applaud actions taken by some of the individual State agencies to address the findings in our audits, we believe that integrity throughout the program cannot be maintained without aggressive, clear, and consistent guidance and oversight from FNS.

We have accepted your management decision for Recommendation Nos. 3a, 3b, 3c, and 4b. In order to reach management decision on the remaining recommendations, please provide us with the additional information as outlined in the OIG Position sections of the report. We recognize that your agency plans to address many of the problems in the CACFP with new strengthened regulations which are currently in the draft proposal stage. We need specific details of how the published proposed rule will address the recommendations.

Also, please reconsider your response to the Recommendations Nos. 1a (disreputable sponsors), 2k (bonding of key sponsor officials), and 3d (administrative costs for sponsors of child care centers). In our opinion, the corrective actions on these three recommendations are critical and need to be implemented as soon as possible to restore integrity to the CACFP. We believe that the changes to the CACFP recommended in this report are urgently needed to prevent even one more sponsor from abusing this important feeding program.

Since the cutoff date (February 19, 1999) for data summarized in this report, we have continued to find more problem sponsors and program abuse. These findings will be presented in future reports.

In accordance with Departmental Regulation 1720-1, please furnish a reply within 60 days describing the corrective action taken or planned and the timeframes for implementation of these recommendations. Please note that the regulation requires a management decision to be reached on all findings and recommendations within 6 months from report issuance.

The Office of the Chief Financial Officer (OCFO), U.S. Department of Agriculture, has responsibility for monitoring and tracking final action for the findings and recommendations. Follow your internal agency procedures in forwarding final action correspondence to the OCFO.

We appreciate the cooperation and assistance provided by the staff from your regional offices and from the State agency officials received during this audit.

ROGER C. VIADERO  
Inspector General

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## **EXECUTIVE SUMMARY**

### **FOOD AND NUTRITION SERVICE CHILD AND ADULT CARE FOOD PROGRAM NATIONAL REPORT ON PROGRAM ABUSE AUDIT REPORT NO. 27601-7-SF**

#### **PRESIDENTIAL INITIATIVE: OPERATION KIDDIE CARE**

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#### **PURPOSE**

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This report presents our analysis of audits and investigations completed as of February 19, 1999, as part of the Presidential initiative known as Operation Kiddie Care. The purpose of this report is to assess the controls in the Child and Adult Care Food Program (CACFP) and their effectiveness in detecting fraud and abuse by individual program sponsors.

Operation Kiddie Care has been underway for about 2½ years. Early audits and investigations provided warning signs that some sponsors participating in the CACFP were not acting in the best interests of the program or of the children they claimed to be feeding. The Inspector General then proposed that the Department undertake an initiative to determine the extent of fraud in the child care program and eliminate it. The Secretary and the Under Secretary for Food, Nutrition and Consumer Services joined the Inspector General in recommending this initiative to the President.

This report presents the status of our work in the CACFP as of February 19, 1999. The report also discusses other major efforts made by a Food and Nutrition Service (FNS) task force as well as actions taken by FNS on recommendations from prior Office of Inspector General (OIG) audits made to correct problems in the CACFP.

Details of 11 OIG investigations of CACFP sponsors have not been included in this report because this information cannot be made

public at this time. Additionally, audits which were initiated after February 19, 1999, are not included in this report.

Our audit and investigative work in the CACFP continues.

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## **RESULTS IN BRIEF**

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Under its current design, the CACFP has attracted opportunistic sponsors who have taken advantage of the program's delivery system, a system that places the primary controls over the CACFP in the hands of the sponsors. Since this program can provide significant monetary gains, many sponsor organizations were created solely for the purpose of acquiring access to the program. While these sponsors have operated as nonprofit organizations, the incentives to enrich themselves at the expense of the program outweighed the goal of making sure that the CACFP is administered as intended; to feed children and adults in day care. This renders the program highly vulnerable to abuse.

As of February 19, 1999, we had completed or had in process reviews in 23 States covering 49 sponsors (includes 1 day care center), 2 employees, and 4 providers. These reviews consisted of 24 audits, 18 investigations, and 13 joint audit and investigations. The following data summarizes the results of our reviews.

- Thirty-seven of the 49 sponsors meet the criteria for being "seriously deficient" in program administration. Serious deficiencies include failure to maintain adequate records, submission of false information to the State agency, a history of administrative or financial mismanagement, and failure to monitor and train providers. These 37 sponsors, who have been receiving approximately \$76.3 million annually in food and administrative funds, are subject to termination from the program if they fail to correct the deficiencies.
- Because 16 of these 37 sponsors were unable to correct their serious deficiencies, they have been terminated from the CACFP. These 16 sponsors were receiving approximately \$34.6 million annually in food and administrative funds.
- Thirty-one investigations for program fraud have been initiated.

- Forty-four individuals have been indicted or named in criminal information documents<sup>1</sup> for defrauding the CACFP; 28 of these individuals have pled guilty or have been convicted; and 26 individuals have been sentenced for illegal activities. (One person is serving a 3-year term and another person was sentenced to serve a 9-year term.)
- Over \$18,000 in fines, \$4.2 million in restitutions, and \$1.1 million in forfeitures have been ordered by the courts.

To put the problem in perspective, the 37 seriously deficient sponsors administered about 14 percent of the total program expenditures in the 23 States where they operated. The 16 terminated sponsors administered about 12 percent of the total program expenditures in the 10 States where they operated. We excluded the funding for independent child care centers from these calculations because these centers were not included in Operation Kiddie Care.

We also concluded that FNS, the Federal agency responsible for administering the CACFP, needs to take more aggressive action to prevent the types of abuses detailed in this report. We found program abuse continuing, even though FNS had information showing significant changes were needed to ensure integrity in the program.

Our reviews show that abuse is widespread in the CACFP. Among the incentives that we believe contributed to abuse of the program were the following:

- The program creates pools of money that invite abuse. Some States allow sponsors to retain food money from child care centers (up to 30 percent of reimbursements) to pay for administrative costs. By contrast, costs for administering day care homes are paid directly to the sponsor and are separate from the homes' food reimbursements. We found that by retaining their centers' food money, sponsors were able to create large pools of funds that remained at their disposal and in many cases directly contributed to the personal enrichment of their officers. We believe that FNS needs to consult with the Office of the General Counsel (OGC) regarding the legality of this practice.

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<sup>1</sup>A criminal information is filed with the court, charging an individual with a crime.

- The program encourages sponsors to ignore provider deficiencies. Sponsors' administrative cost reimbursements are based on the number of providers they administer, and providers' reimbursements are based on the number of meals they serve. Strict enforcement of meal claims can reduce a provider's potential income and cause the provider to seek a less conscientious sponsor. Consequently, sponsors have a financial incentive to ignore provider deficiencies. Our unannounced visits to over 3,200 providers and centers nationwide have shown that, generally, providers and centers we visited were claiming more meals than they were serving.
- Sponsor officials may increase their salaries by reducing funds for day care monitoring activities. Sponsors employ monitors to travel to homes and centers to help ensure that meals are properly constituted and that meal claims are accurate. However, sponsors are under no obligation to employ a number of monitors commensurate with the number of homes they sponsor. We found sponsors hiring fewer monitors so that more administrative funding could be spent on officers' salaries and benefits.

Over the last four years, reports and recommendations made by OIG and by FNS' own task force have made FNS aware that significant regulatory changes were needed to ensure integrity in the CACFP. Since 1995, FNS has been drafting proposed changes to the CACFP regulations (7 CFR Part 226) to improve management and integrity in the CACFP. FNS estimated in its 1998 Federal Managers' Financial Integrity Act (FMFIA) that the implementation of these regulations will be delayed until the end of fiscal year 2000.

Although FNS has been conducting periodic training of States and sponsors and has issued a CACFP State and Sponsor Management Improvement Guide, these actions have not been an adequate safeguard against program mismanagement. We believe that if FNS had been more diligent in implementing the needed regulatory changes, it could have prevented or detected much of the fraudulent activity we found during our audits and investigations.

Because the CACFP's delivery system depends on the sponsors' oversight, and because many sponsors have demonstrated a lack of integrity in that oversight, FNS needs to determine if the current system should be retained. We are recommending that FNS strengthen integrity in the program through two concurrent actions.

To provide a short-term corrective, FNS should immediately implement recommendations previously set forth by OIG and the FNS task force, as well as the other recommendations we make in this report to establish controls over the present delivery system. Simultaneously, to establish a long-term solution, FNS should determine if an alternative delivery system would better serve the needs of the program.

We also noted three other areas where improvements in the CACFP are needed.

- Sponsors do not have clear directions for determining what administrative costs could be paid from CACFP funds. Many sponsors and State agencies honestly did not understand the program. Either the sponsors did not know which rules to follow, or the States did not know which rules to enforce. FNS needs to develop a sponsor handbook on the administrative management of the CACFP.
- FNS needs to establish better coordination between two of its programs, the Food Stamp Program (FSP) and the CACFP. Providers can be eligible for larger payments from the CACFP if they are on the Food Stamp Program. However, we found that some of these providers were not disclosing their CACFP income to Food Stamp Program eligibility workers, thereby receiving excessive benefits from each of these FNS programs. In a cursory review in two States, we found 14 cases of potential FSP fraud.
- FNS needs to provide clearer direction about how State agencies should recover CACFP funds from sponsors who have made inaccurate, ineligible, or fraudulent claims. The methods used by some State agencies hurt the providers, centers, and children who are not responsible for the overpayments. These State agencies collect overpayments due from the sponsors by offsetting future food reimbursements to the centers and providers serving meals to eligible children. In effect, the children are shortchanged twice, while the perpetrators of the overclaims retain their ill-gotten gains.

We also believe that FNS should take advantage of the public's presence at provider sites. Parents of the children in day care seem to be unaware that their children are participating in the CACFP and are due the benefits of the program. FNS needs to raise the visibility



of the CACFP to encourage parental involvement by posting some type of program notification at the providers' home or child care centers.

Our work on Operation Kiddie Care is continuing. Since February 19, 1999, the cut-off date for data used in this report, we have continued to find sponsors abusing and possibly defrauding the CACFP. We will be reporting on additional cases at a later date.

We have also issued three audit reports on the administration of the CACFP by the California Department of Education. These reports, 27601-6-SF, 27601-8-SF, and 27601-9-SF, are available on the OIG web page ([www.usda.gov/oig/](http://www.usda.gov/oig/)).

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## **KEY RECOMMENDATIONS**

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We are recommending that FNS study alternative methods of delivering a meal program to children and adults, specifically one that addresses the problems we found in the private, nonprofit organizations included in our reviews. We are also recommending that while the study is underway and the program continues in its current form, FNS strengthen controls by implementing as soon as possible the recommendations put forth in earlier OIG reports and in the results of FNS' task force. These recommendations respond to the problems we found during Operation Kiddie Care and include the development of standards for approving new sponsors, renewing continuing sponsors, and terminating deficient sponsors. We are also restating our recommendation that FNS provide a different method of reimbursing administrative costs so the reimbursement is not based on the number of the sponsor's providers, a method that creates a disincentive to effective compliance.

Other recommendations are aimed at strengthening current controls: we are recommending that FNS

- develop a handbook that incorporates all Federal regulations controlling sponsorship of the program and that identifies the costs that are allowable,
- clarify what constitutes adequate sponsor staffing and adequate provider training,

- raise the visibility of the CACFP by ensuring that parents know their day care providers are participating in the program, and
- obtain an opinion from The Office of the General Counsel on the legality of the sponsor practice of retaining a portion of the food money earned by centers as the sponsor's compensation for administering the program. If this practice is determined to be legal, FNS should establish a realistic rate that sponsors can retain for administering the program to child care centers and tell centers what this amount is.

We are also recommending that FNS issue guidance to States so that the recovery of ineligible program funds from sponsors comes from the sponsors' funds and not monies for children's meals.

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## **AGENCY POSITION**

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In its response to the official draft, FNS states that it is committed to improving the operations of the CACFP and will continue to aggressively pursue all means to ensure sound program management and prevent fraud. FNS' response is reproduced as exhibit E to this report.

The agency's responses to the individual recommendations are included after each recommendation in the report, along with our comments. We do not believe that the corrective actions proposed to date by FNS go far enough to correct the serious problems in the CACFP, and in our comments we put forward the specific actions we believe are needed.

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# INTRODUCTION

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## BACKGROUND

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The Child and Adult Care Food Program (CACFP) is designed to ensure that children and senior citizens in day care facilities receive nutritious meals (see photo no. 1). Program funding nationwide for fiscal year 1996 was \$1.58 billion. For fiscal year 1997, the appropriation was increased by about 10 percent to \$1.74 billion.

The program is administered at the Federal level by the Food and Nutrition Service (FNS) and at the State level by a State agency. State agencies administer their programs through public or nonprofit sponsoring organizations which act as a liaison between the State agency and participating day care facilities. Sponsors are ultimately responsible for program operations in those facilities.



PHOTO NO. 1 - CHILDREN IN DAY CARE ENJOYING A MEAL.

Facilities eligible to participate include day care homes (homes) or child care centers (centers). A home is a day care facility located in a private residence. The operator of the home is referred to as the "provider." A child care center is operated by a public or private nonprofit organization, is licensed to provide child care, and primarily serves pre-school children. Homes and centers must be licensed by a State or local licensing authority.

Under Title 7 Code of Federal Regulations (CFR) 226.4(h) funding is authorized to States specifically for the purpose of conducting audits and administrative reviews of institutions. These funds are designated to pay the cost of required organizationwide or program-specific audits of institutions. Title 7 CFR 226.6(l) also specifies that State agencies perform administrative reviews of sponsors on a periodic basis.

Operation Kiddie Care is a national initiative to identify, investigate, and prosecute individuals who are abusing and defrauding one of the most important feeding programs in USDA, the Child and Adult Care Food Program. OIG uses a "sweep" audit approach to determine if CACFP sponsors are in compliance with CACFP regulations. A "sweep" is an audit approach used to gain an accurate picture of an enterprise's operation in a brief, unguarded moment. During a "sweep", auditors and investigators conduct simultaneous, unannounced visits to selected audit sites, so that a realistic picture of a site's operation can be determined.

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## **OBJECTIVES**

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Our audit objectives were to (1) conduct an intensive review of sponsors whom we have identified as potential problem sponsors, (2) identify the types and magnitudes of the abuses in which the identified sponsors were engaging, (3) provide data to FNS and the State agencies to effect claims and/or other sanctions against sponsors who are abusing the program, (4) refer cases of potential fraud to OIG-Investigations, and (5) identify control weaknesses in the program that had rendered it vulnerable to fraud and other abuses.

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## SCOPE

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The scope of our review for this report was the sponsors participating in the CACFP during the period January 1996 to February 1999. Some of the sponsors also selected for review had terminated their participation in the CACFP during this period. At the time of our review, there were approximately 1,200 sponsors of day care providers and day care centers participating in the program. As of February 19, 1999, we had in process or had completed a total of 37 audits and 31 investigations of child care sponsors, employees and providers (see figure 2). Thirteen of these cases were joint audits and investigations.

The sponsors were selected for an audit and, if necessary, an investigation based on a problem-sponsor profile we developed and referrals from FNS, State agencies, or other sources (whistleblower complaints, audit leads, etc.).

Audit work was performed from January 1996 through August 1998 at the FNS Western Regional Office in San Francisco, California; the FNS Southwest Regional Office in Dallas, Texas; the FNS Mountain Plain Regional Office in Denver, Colorado; the FNS Midwest Regional Office in Chicago, Illinois; the FNS Southeast Regional Office in Atlanta, Georgia; the FNS Mid-Atlantic Regional Office in Robbinsville, New Jersey, the FNS Northeast Regional Office in Boston, Massachusetts; and the State agencies in each OIG region (see figure 1). We also conducted work at the FNS National Office.

Fieldwork included audits and investigations of 55 child care sponsors, day care centers, employees, and providers located in 23 States. We also attempted to visit over 3,200 day care homes and centers (see exhibit D). We actually visited 2,805 homes and centers; 483 could not be visited because they were no longer in the program or no one was on the premises during the stated food service hours.

We conducted the audit in accordance with generally accepted government auditing standards.



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## METHODOLOGY

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To accomplish our objectives and support our findings, we performed the following steps:

- We interviewed FNS Regional Office staff to identify problem sponsors.
- We interviewed FNS Regional Office staff to identify regional policies or procedures relating to the program.
- We interviewed State agency staff to determine the universe of sponsor data.
- We reviewed State agency files to obtain information about the sponsors' operations and funding.
- We interviewed the sponsors' staffs to obtain an understanding of their operating procedures.
- We reviewed each sponsor's records supporting its claims for reimbursement, its receipt and disbursement of program funds, and its overall administration of the program. Records we reviewed included receipts, cancelled checks, bank statements, provider claims (meal counts), provider menus, enrollment forms, monitoring checklists, and training documents.
- We interviewed the certified public accountants who audited the sponsors' program claims (when applicable).
- We judgmentally selected homes or centers operating under the sponsors and completed reviews at the provider sites. Criteria for the judgmental sample were as follows: (1) providers with a high reimbursement, (2) providers with high enrollment, and (3) providers who consistently claim the same number of children for meals.
- At each of the homes or centers, we interviewed providers or other persons present and reviewed their records.
- We also conducted interviews and record reviews at the FNS National Office.

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## FINDINGS AND RECOMMENDATIONS

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<b>I. PROGRAM CHANGES ARE NEEDED TO ENSURE INTEGRITY IN THE CACFP</b>
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The delivery structure of the CACFP entrusts sponsors with program oversight, but we found that many sponsors, particularly private nonprofit organizations, lacked the integrity needed to protect the CACFP from abuse. While FNS had information showing problems existed, it had not acted aggressively to impose stronger controls. In 1995, OIG audits found day care homes claiming meals for nonexistent children; more recently, under Operation Kiddie Care, investigations have found sponsors forging documents to increase their administrative reimbursements.

As a result of Operation Kiddie Care, 16 sponsors nationwide have been terminated from the program because of serious deficiencies, and 28 individuals have pled guilty or have been convicted of fraud. Investigations disclosed that sponsors had created fictitious providers, inflated meal counts, and diverted program funds. The results of investigations have been significant. For example, the indictment for one sponsor included 117 counts of fraud. Two other audits and investigations resulted in indictments, convictions and sentencing of sponsor officials; one is serving a 3-year prison term and another was sentenced to serve a 9-year term.

This will be the fourth report issued since 1995 that has documented significant problems in the CACFP. OIG will have issued three reports: a nationwide report of CACFP deficiencies in March 1995 (audit no. 27600-6-At); the Operation Kiddie Care interim report issued to the Secretary in April 1998 (audit no. 27601-3-SF); and this current audit report (audit no. 27601-7-SF). The fourth report was from an internal FNS task force made up of FNS national and regional personnel and State agency personnel who made 33 recommendations to change the CACFP in July 1995.

These reports and recommendations made by OIG and by FNS' own task force have made FNS aware that significant regulatory changes were needed to ensure integrity in the CACFP. Since 1995, FNS has been drafting proposed changes to the CACFP regulations (7 CFR Part 226) to improve management and integrity in the CACFP. FNS estimated in its 1998 Federal Managers' Financial Integrity Act (FMFIA) that the implementation of these regulations will be delayed until the end of fiscal year 2000.

While FNS has been conducting periodic training of States and sponsors and has issued a CACFP State and Sponsor Management Improvement Guide, we believe that if FNS had implemented the needed regulatory changes, the additional controls in the program could have prevented or detected much of the fraudulent activity we found during our audits and investigations.

We concluded that FNS needs to ensure integrity through two concurrent actions: it should immediately implement recommendations previously set forth by OIG and the 1995 FNS task force (short-term corrective actions), and with these controls in place, it should determine if an alternative delivery system to the one now in effect (long-term corrective action) is necessary.

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**FINDING NO. 1**  
**FRAUD AND ABUSE**  
**REVEAL THE NEED**  
**FOR PROGRAM REDESIGN**

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We found CACFP sponsors operating as nonprofit organizations, but enriching themselves at the expense of the children to whom they were supposed to provide meals.

Under the CACFP's design, FNS and the States depend upon sponsors to enroll providers in the program, monitor provider operations, determine the accuracy of provider claims, and distribute Federal reimbursements for meals served. FNS and the State must rely on the integrity of the sponsors to ensure that Federal funds are protected from abuse, yet because the sponsor's administrative fee is based on the number of homes enrolled and the number of meals served, and because there is little State oversight of sponsor activities, there are few incentives for sponsors to provide cautious oversight. We found that some sponsors, particularly private, nonprofit organizations, lacked the integrity needed to ensure the protection of Federal funds.

To date, Operation Kiddie Care has found 37 sponsors who have met the FNS criteria of being "seriously deficient" in program administration and are subject to termination from the program if they fail to correct the deficiencies. These 37 sponsors have been receiving approximately \$76.3 million annually in food and administrative funds.

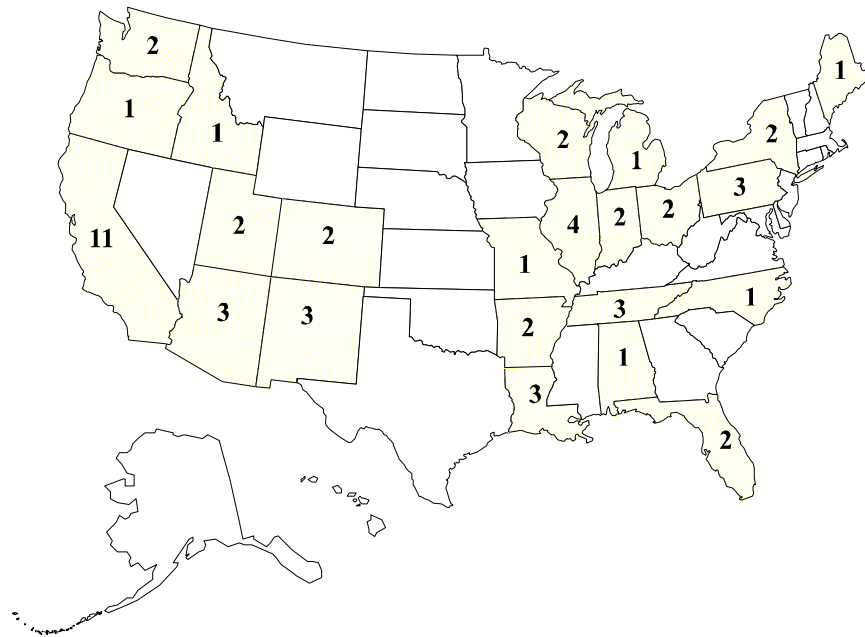
To put the magnitude of the problems we have found in perspective, the \$76.3 million paid to these 37 seriously deficient sponsors, is about 5 percent of the average 1996 and 1997 program expenditures of \$1.4 billion in all States receiving CACFP funding, and is about 8 percent of the average 1996 and 1997 program expenditures of \$919 million in the 23 States where we conducted our audits and investigations.

As stated, our audits and investigations have concentrated on day care providers and day care centers that are administered by a State agency through a sponsoring organization. About 41 percent of the total program expenditures (\$605 million of \$1.4 billion) however, is paid to independent child care centers that are administered directly by State agencies.

If we exclude these centers from our percentages (because we have not been including them in Operation Kiddie Care), the seriously deficient sponsors we found represent about 14 percent of the total program expenditures in the 23 States where we conducted our audits and investigations.

Thirty-one investigations of program fraud have been initiated, and 16 of the 37 sponsors found to be seriously deficient have been terminated from the CACFP. The program expenditures received by these 16 sponsors (\$34.6 million annually) total about 12 percent of the total program expenditures in the 10 States where these sponsors were operating, excluding the funding for independent child care centers.

**Figure 1: Number of Locations Reviewed, by State**



**AUDITS AND INVESTIGATIONS**

As of February 19, 1999, we have issued 27 audit reports on sponsors participating in the CACFP. As of that date, an additional 6 audits were in process, as were many of the 31 investigations. A summary of the results of our audits and investigations, by State, follows.

Some of these investigations technically started before the initiation of Operation Kiddie Care. The results of all audits and investigations, however, are presented here because they demonstrate the type and magnitude of the problems in the CACFP.

## **Alabama**

### **Quad County Child Nutrition Program, Audit No. 27010-2-At**

We reviewed Quad County Child Nutrition Program of Decatur, Alabama, at the request of the State agency. We determined that the sponsor met the FNS criteria of being seriously deficient in its administration of the program.

Of the 115 providers we reviewed, 53 overclaimed reimbursements totaling \$3,088 either for meals not served or for unauthorized or ineligible meals. The providers claimed meals for days we found them closed and for children we determined were absent. In addition, we noted compliance deficiencies involving improper record maintenance, expired provider eligibility determinations, and license capacity violations. The State and sponsors' oversight of day care home providers was not sufficient to prevent and detect material compliance deficiencies and overclaims.

## **Arizona**

### **Employee of Feeding Arizona Kids, Inc., Phoenix, Arizona (Investigation only)**

An investigation was initiated based on an allegation that the former office manager diverted money from the CACFP to her own use. The former office manager of an Arizona CACFP sponsoring agency was placed on probation for 5 years and was ordered to pay FNS \$31,900 in restitution after she pled guilty to theft of Government money. Our investigation disclosed that the manager diverted money by writing 61 checks on the sponsoring agency's account, made payable to individuals whom she had falsely represented as day care providers. She then deposited all but one of these checks into her personal account.

### **Feeding Arizona Kids, Inc., Audit No. 27010-6-SF**

We reviewed Feeding Arizona Kids, Inc., of Phoenix, Arizona, based on information provided by the State agency and our analysis of State agency files. We determined that the sponsor met the FNS criteria of being seriously deficient in its administration of the program.

We questioned \$45,409 in unallowable, unapproved, or unsupported expenditures. About half of this amount was paid for employee benefits, while about \$3,600 was paid as consulting fees to board members or employees. Also, the sponsor did not adequately train and monitor its providers.

#### **B J Enterprises, Inc., Audit No. 27010-7-SF**

We reviewed B J Enterprises, Inc., of Scottsdale, Arizona, based on our analysis of sponsor files maintained by the State agency. We found the sponsor to be seriously deficient in its administration of the program.

We questioned \$8,322 in unallowable and unsupported administrative costs. We also concluded that the sponsor failed to adequately monitor program operations in its day care homes, which may have contributed to the meal overclaims submitted by providers.

### **Arkansas**

#### **Operation Kids, Inc., Audit No. 27601-6-Te**

Operation Kids, Inc., of Camden, Arkansas, was selected for review based on our risk assessments of six sponsors whose files we reviewed at the State agency. In addition, Operation Kids, Inc., was identified to us by the State agency as a potential audit candidate. We did not identify any significant program abuses by this sponsor. However, we did find that over 20-percent of the providers had not received the required annual training. The sponsor did not have a system in place to track provider training.

### **California**

#### **Angela's Angels Preschool, Inc., Audit No. 27010-2-SF**

Angela's Angels Preschool, Inc., of Visalia, California, was one of the first CACFP sponsors we reviewed and was the precursor to our nationwide review of CACFP sponsors. FNS referred this sponsor to us based on an anonymous complaint received by another State agency and passed along to the California State Department of Education (CDE).

Based on our audit results, the sponsor was found to be seriously deficient in administration of the CACFP and was terminated from the program. The sponsor's onsite reviews of its providers were not thorough and were always announced in advance, and all required reviews were not conducted. The sponsor did not keep accurate and complete records and did not adequately review and verify the providers' claims for reimbursement. The sponsor also did not disburse program funds to providers in a timely manner.

The husband and wife who owned and operated the business were charged in a 23-count Federal indictment and were subsequently arrested. The charges included conspiracy, perjury, obstruction of justice, and mail fraud.

It is alleged that the couple paid themselves reimbursements for meals claimed on behalf of providers who no longer participated in the program, paid meal reimbursements to full-time employees based on false claims which the employees submitted, and created false home inspection reports to conceal the fact that employees were not making required home inspection visits. They are awaiting trial.

Three of the couple's former employees have already pled guilty to mail fraud charges associated with the submission of false day care home provider claims. These 3 employees were each sentenced to 5 years' probation and 90 days home detention and each ordered to pay USDA \$12,000 in restitution.

#### **Pacific Asian-American Family Care, Inc., Audit No. 27010-4-SF**

We reviewed Pacific Asian American Family Care, Inc., of Long Beach, California, at the request of the California State Department of Education, which had expressed concerns about the sponsor's operation. Based on the results of our audit, the sponsor was found to be seriously deficient in administration of the CACFP and was terminated from the program.

Specifically, the sponsor failed to provide support for the administrative costs it claimed. Furthermore, the limited records we were provided indicated that excessive and unallowable personal expenses may have been charged to the program. As a result, we questioned all of the \$3.3 million paid to the sponsor for reimbursement of administrative costs from 1991 through 1996.



The wife was also a manager for the State Department of Education, which was responsible for administering the program. As a manager for the State, the wife was responsible for overseeing this and other sponsors in Southern California.

Criminal charges were filed against the husband and wife who owned and operated this sponsorship. The couple was charged with defrauding the program of approximately \$2.2 million by submitting inflated budgets and by diverting CACFP funds to themselves through "payments" to nonexistent employees and bogus business entities.

Following their guilty pleas, the husband was sentenced to 2 years in Federal prison and the wife to 3 years. They were ordered to pay the Government \$2.2 million in restitution and forfeited four properties they owned, including their 5,000 square-foot home in an exclusive neighborhood in Southern California (see photo no. 2).



**PHOTO NO. 2 - 5,000 SQUARE-FOOT HOME FORFEITED BY PAAM, A CALIFORNIA CACFP SPONSOR.**

Another property located in Southern California (see photo no. 3) which sold for \$415,000, was forfeited by the sponsor.



PHOTO NO. 3 - ANOTHER HOME (SOLD FOR \$415,000) FORFEITED BY PAAM, A CALIFORNIA CACFP SPONSOR.

The sponsor's former executive director and program director engaged in a separate fraud scheme. They submitted false claims for nonparticipating providers, and, as a result, the sponsor was reimbursed in excess of \$60,000 for these claims. The executive director and program director used these funds for their own personal use. Following their guilty pleas, they were each sentenced to 7 months in prison, 3 years' probation, and ordered to pay a total of \$60,000 in restitution.

**Community Business Improvement Association, Inc., Audit No. 27010-9-SF**

Community Business Improvement Association, Inc., of Pasadena, California, was selected for review based on a whistleblower complaint. The sponsor was found to be seriously deficient in its administration of the program.

The former manager of the sponsor admitted to having misappropriated CACFP funds by submitting false claims for a nonexistent provider. The former manager and an accomplice pled

guilty to making a false statement in connection with CACFP provider claims. They conspired to create a fictitious child care provider and illegally obtained over \$23,000 in CACFP funds. They were each sentenced to 3 years' probation and 6 months in a home detention program, and ordered to pay a \$100 fine. They were also ordered to pay the total restitution amount of \$23,340. The investigation also disclosed that a former California Department of Social Services employee furnished the former manager with a fictitious State child care license.

The sponsor's former manager herself admitted to falsifying home inspection reports for 20 to 50 percent of the required home visits.

We also questioned administrative costs totaling \$462,387. The sponsor claimed unsupported payroll costs of \$372,613, most of which was paid to the executive director and three other key employees, all of whom were related. The sponsor also claimed an estimated \$59,800 in rent that was unallowable because the property was owned by the executive director and her husband. The sponsor claimed about \$11,000 in vehicle lease costs it could not support, and it received \$18,000 in program funds it could not account for.

Furthermore, the three employees were engaged in non-program activities. The executive director and the accountant apparently operated a bail bonds business from the same location that housed the sponsor's offices (see photo no. 4). Although the executive director said that business was operated from their home, she acknowledged that the bail bonds telephone number rang both at the office and at their home. Furthermore, we noted that the office building's signs clearly marked it as a bail bonds business (also offering income tax, fax, and notary services).



PHOTO NO. 4 - BUILDING OWNED BY CBIA'S EXECUTIVE DIRECTOR AND HER HUSBAND SHOWING BAIL BOND AND OTHER SERVICES AVAILABLE ON FIRST FLOOR. CACFP OFFICES WERE LOCATED ON THE SECOND FLOOR.

The sponsor also failed to pay all its providers and centers within the time period allowed.

#### **Aladdin Child Care Services, Audit No. 27010-11-SF**

We selected Aladdin Child Care Services (Aladdin) of Inglewood, California, after an OIG auditor pursued a lead on a complaint made against the sponsor. We obtained Aladdin's records with a subpoena when we found out that the sponsor was removing itself from program participation while still owing its day care centers thousands of dollars in food reimbursements. The sponsor met the criteria of being seriously deficient in its administration of the program.

We found that this sponsor, before terminating itself from participation in the CACFP, used funds for unsupported and unallowable purposes. Although an absence of records prevented us from quantifying all of its questionable activities, we still identified about \$800,000 in questionable costs and payments. The majority of day care centers were not paid for all meal reimbursements they were

entitled to, and if they were paid, they were not paid on time. While the sponsor underpaid many of its day care centers, it usually overpaid the day care center that it owned. We found a large amount of unexplained payments to the sponsor's own day care center. The sponsor also used CACFP funds to pay for questionable administrative costs, such as construction costs, overdraft charges, and attorney fees.

In October 1997, CDE issued an audit report on this entity covering fiscal years 1994 through 1996 and issued a qualified opinion because of "a material overpayment of reimbursements to the centers and agency" and "material noncompliance." However, the CDE did not believe the findings were material enough to terminate the sponsor from the CACFP.

Even though CDE knew about Aladdin's questionable activities as early as January 1997, it did not take the necessary steps to correct these deficiencies or terminate Aladdin's participation in the CACFP. In fact, Aladdin received approximately \$460,000 in program funds after CDE became aware of these deficiencies. We also found that Aladdin began paying centers even less of the total meal reimbursements due them after CDE became aware of the sponsor's problems.

### **Children's Spectrum Child Care Services, Inc., Audit No. 27010-13-SF**

Children's Spectrum Child Care Services, Inc., of Yucca Valley, California, was originally selected by OIG because it oversees a large number of homes and centers, and because it fit our profile of a problem sponsor (it claimed 30 percent of day care center food reimbursements to cover administrative costs--see Finding No. 3). Subsequently, in response to our request to each of the States for potential review candidates, the CDE suggested this sponsor for review.

This sponsor was found to be seriously deficient in its administration of the program, especially in the area of claimed administrative expenses. We questioned over \$231,000 in administrative costs paid to or on behalf of the sponsor's administrative director. We also found that the sponsor did not adequately support the allocation of costs between its administration of day care homes, which offered a

fixed reimbursement, and its administration of day care centers, which offered a much larger reimbursement.

While residing and working in Wisconsin, the executive director claimed a salary from the California sponsorship and had the exclusive use of a leased vehicle that was charged to the program (see photo no. 5). We also determined that for a 6-month period, the executive director received Unemployment Compensation Benefits from Wisconsin despite receiving his salary from the sponsorship in California.



**PHOTO NO. 5 - VEHICLE LEASED BY CHILDREN'S SPECTRUM WITH CACFP FUNDS. PARKED AT WISCONSIN LOCATION WHERE CHILDREN'S SPECTRUM'S EXECUTIVE DIRECTOR HAD ANOTHER FULL-TIME JOB.**

A criminal complaint has been filed in Wisconsin against the executive director for allegedly receiving unemployment benefits in Wisconsin while being employed full-time in California as the executive director of a CACFP sponsor.

### **A Perfect Balance, Inc., Audit No. 27010-14-SF**

We selected A Perfect Balance Inc., of Diamond Bar, California, for review because, like Children's Spectrum, it used day care center food reimbursements to cover administrative costs. The sponsor was found to be seriously deficient in its administration of the program. The sponsor delayed over \$40,000 in meal reimbursement to its centers and homes, and claimed over \$6,000 in unallowable or unsupported administrative costs. We also determined that the sponsor had not paid creditors when bills were due even though the sponsor had requested and received an administrative advance. The sponsor also did not properly staff the office during normal business hours.

### **Sunshine Family Day Care Services, Inc., Fallbrook, California (Investigation only)**

The sponsor is currently not participating in the CACFP and is being investigated for program fraud. It appears that the sponsor fraudulently claimed administrative funds. The State agency initiated the investigation by seizing the sponsor's records through a search warrant.

Criminal charges were filed against the husband, wife, and daughter who owned and operated this sponsorship. A 10-count indictment was filed against the three defendants for mail fraud for fraudulently obtaining over \$95,000 from the State agency and the CACFP. The defendants used various schemes to inflate claims for reimbursement and also falsified reports to make it appear that they were properly monitoring approximately 1,000 day care homes which they sponsored.

### **Child Care Coordinating Council of Northern California (Investigation only)**

An investigation was initiated following the confession of the executive director. The sponsor was terminated from the program in April 1995 and was investigated for program fraud. The former director confessed to submitting false invoices to the State agency and using the illegally obtained CACFP funds to pay nearly \$300,000 to three individuals for bogus salaries and consulting services. These three individuals whom the former director paid pled guilty to mail

fraud and were sentenced to prison. The former director also pled guilty to submitting false claims and was sentenced to 2 months in community confinement, 2 months home detention, and ordered to pay \$306,000 restitution.

This investigation was initiated prior to the start of Operation Kiddie Care.

## **Florida**

### **Family Day Care Services, Inc., Audit No. 27601-7-At**

Family Day Care Services, Inc., (FDS) of West Palm Beach, Florida, was selected for review based on the recommendation of the State agency. The State agency had identified material compliance deficiencies with FDS' administration of the program and received complaints from providers and legislators regarding FDS delays in payment of provider claims. The fact that FDS was the largest nongovernmental affiliated sponsor was also a criterion in our selection.

Based on the results of our audit, the sponsor was found seriously deficient in administration of the CACFP and was terminated from the program. FDS inflated claims it submitted to the State for meal reimbursements and did not maintain adequate accounting and other fiscal records to support its administrative costs. We questioned \$123,730 in meal reimbursements paid to FDS due to inflated monthly claims, and \$197,747 of the administrative costs paid to FDS due to its failure to provide fiscal records to support the cost.

FDS also failed to adequately monitor the operations of its providers. As a result, providers claimed excessive reimbursement for meals not served and for ineligible meals. In addition, the sponsor did not provide annual training to its providers.

## **Idaho**

### **Kiddie Korner Kid Kare, Inc., Idaho (Investigation only)**

An investigation was initiated based on State agency concerns regarding suspected fraud by the director. The director of two centers submitted false claims totaling \$83,000. She was sentenced to serve



8 months in prison followed by 3 years of probation. She was also ordered to pay \$62,951 in restitution and \$100 in fines. The court further ordered her to relinquish her day care license and not reapply for 5 years, during which time she was to refrain from any participation in child care, whether paid or unpaid.

## **Illinois**

### **Ken-Kia Child Development, Inc., Audit No. 27010-10-Ch**

Ken-Kia Child Development, Inc., of Hazelcrest, Illinois, was selected for review based on State agency concerns regarding its administration of the program, and on the size of its operation. This sponsor met the criteria of being seriously deficient in its administration of the program.

Our unannounced visits to day care home providers disclosed that the sponsor's monitoring visits were generally ineffective in assessing compliance with program requirements. We found that providers did not maintain adequate records. Unsupported meal claims totaled \$14,568 for the month under review. Some providers even claimed meals for children who were not present during our visits. We also found that providers claimed meals on days when they were not actually in operation or when they were caring only for their own children.

We noted sanitation and safety deficiencies at some providers, and found providers who did not comply with licensing requirements and exceeded their authorized capacity. Finally, the sponsor did not require that day care providers attend annual training sessions.

### **YWCA of Metropolitan Chicago, Audit No. 27601-17-Ch**

YWCA of Metropolitan Chicago, Illinois, was selected for review based on problems identified by the State agency. The sponsor met the criteria of being seriously deficient in its administration of the program.

The YWCA needed to perform more timely and thorough monitoring visits of its providers. Eighty-nine percent of the providers we reviewed did not maintain adequate records of the number and/or type of meals being served. In addition, 43-percent of the providers

claimed meals served (1) for children who were absent or were not enrolled in the program, (2) for days when only their own children were present, or (3) for days on which they did not provide service. One provider claimed meals served at an address which we discovered to be vacant.

We attributed the deficiencies to inadequate monitoring and training on the part of the sponsor. This sponsor did not perform and/or document that it had performed the required monitoring and could not provide evidence that it had properly trained the providers.

### **Human Development Center, Audit No. 27601-18-Ch**

Human Development Center of Harvey, Illinois, was judgmentally selected for review. The sponsor met the criteria of being seriously deficient in its administration of the program. Specifically, the sponsor's monitoring visits were generally ineffective in assessing compliance with program requirements. Providers did not maintain adequate records of the number and type of meals being served and claimed meals for children who were absent or were no longer participating in the program. Some providers also claimed meals that were served to their own children at times when no other children were present, or were served on days when they were not in operation. At least one provider claimed meals for an unlicensed location.

The sponsor's reviews of providers' monthly meal claims were not adequate to disclose the problems we identified in our review.

### **Louisiana**

#### **Sage Community Providers, Inc., Audit No. 27601-5-Te**

Sage Community Providers, Inc., of New Orleans, Louisiana, was selected based on our risk assessment of two sponsors referred by the State agency and on advice from the Office of Inspector General, Investigations. The sponsor was found to be seriously deficient in its administration of the program and terminated itself from the CACFP.

We reviewed the sponsor's bank statements for a 7-month period and questioned whether \$34,800 in checks to 45 providers was for

legitimate meal reimbursements. The checks did not appear to have been received by the providers as reported by the sponsor.

The sponsor also failed to provide adequate support for all administrative costs claimed and did not limit claims to actual expenses when the maximum allowable per-home claim was greater. We questioned over \$18,000 in administrative costs claimed.

The sponsor did not adequately monitor its providers' operations. The reviews were not thorough, and many may not have been conducted. Of 525 sponsor monitoring visits, only 1 percent indicated problems with the providers; by contrast, of the providers visited by OIG, 35-percent made claims on days when they were not home or had no children in their care. Eighty-six percent of the providers we visited received excessive meal reimbursements totaling over \$9,000. These overpayments occurred because the providers failed to comply with program and recordkeeping requirements.

#### **Lunch, Inc., Audit No. 27010-3-Te**

Lunch, Inc., of Baton Rouge, Louisiana, was selected for review based on recommendations of the FNS regional office and concerns of Louisiana State agency officials. We did not identify any significant program abuses by this sponsor. However, we did identify several conditions that required corrective action.

Thirteen providers had not obtained the required annual training and consequently did not meet the State's registration requirements. The sponsor was ineligible for the \$840 in administrative reimbursement it received while the providers were out of compliance.

During our home visits, we found that ten of the providers did not keep their records current. Also, some providers claimed meals for days when no one was home during our attempted visits or for children we did not observe in attendance on the day of our visit.

## **Maine**

### **Southern Maine Christian Day Care Services, Audit No. 27010-13-Hy**

Southern Maine Christian Day Care Services of Gorham, Maine, was reviewed as part of the nationwide review of CACFP sponsors. The sponsor was found to be seriously deficient in its administration of the program. Our unannounced visits to providers and a statistical review of the providers' claims for reimbursement disclosed widespread noncompliance with meal counting and service regulations.

The sponsor did not effectively administer either provider or financial operations and failed to correct reported accounting system deficiencies. We identified related-party financial transactions of over \$393,000 that were not allowable or reasonable. The primary cause of these deficiencies was the sponsor's ongoing disregard for regulations governing program operations and the allowability of administrative costs.

## **Michigan**

### **MAJCO, Inc., Detroit, Michigan (Investigation only)**

An investigation was initiated based on a complaint made by an employee of the sponsor. A former city school board member and her assistant were indicted for falsifying claims from 16 day care centers the board member owned and operated. The investigation determined that between 1980 and 1993, the centers defrauded USDA of approximately \$27 million in CACFP funds. The investigation disclosed that the board member and the assistant inflated meal count sheets and falsified supporting documentation. A food vendor admitted supplying false invoices to inflate the day care centers' food costs to substantiate the false meal count sheets. The board member has been convicted for fraudulently obtaining \$15.5 million in CACFP funds.

This investigation started before the initiation of Operation Kiddie Care. The results are included in this report, however, because it demonstrates the type and magnitude of the problems in the CACFP. Prior to prosecution, MAJCO was terminated by the State agency.

## **Missouri**

### **Child Nutrition Services, Inc. Audit No. 27010-1-KC**

Child Nutrition Services, Inc., of Gladstone, Missouri, was selected based on FNS regional office response and a review of sponsor records at the State agency. We did not identify any significant program abuses by this sponsor. However, we did identify several conditions that require corrective action.

Problems existed with the sponsor's monitoring and training of providers. We questioned meal claims by providers who, during our visits, were behind in their meal counts or who, also during our visits, had completed their meal claim records ahead of the meal served. Eight providers had unreasonable meal claims. We questioned over \$12,000 in meals claimed by the providers we visited. We eventually billed and collected almost \$7,500 associated with the questionable meals claimed.

## **New Mexico**

### **Connections, Inc., Audit No. 27010-04-Te**

Connections, Inc., of Gallup, New Mexico, was randomly selected for review from a group of sponsors with 200 or more day care home providers. The sponsor was found to be seriously deficient in its administration of the program.

We found various problems with the providers: they were not at home at the time of our visits, they did not keep their records current, they claimed meals for children not present, and they claimed nonresident children as residents to circumvent State licensing regulations. We questioned about \$6,000 related to these problems for the month of our review.

We also found various problems with the sponsor: monitors did not report attendance and menu recordkeeping violations; the sponsor improperly charged more administrative costs to the CACFP than to the other State and local programs it operated; and the sponsor did not ensure that providers received required annual training.

**Employee of Families and Youth, Inc., Sunland Park, New Mexico  
(Investigation only)**

An investigation was initiated based on a referral from the General Counsel, New Mexico Children, Youth and Families Department. Our investigation disclosed that a site representative forged and negotiated 68 checks issued to day care providers and altered computerized records to increase payments to some providers. She was placed on supervised probation for 5 years, and ordered to pay \$17,426 in restitution.

**North Carolina**

**Cape Fear Tutoring, Inc., Audit No. 27601-4-At**

Cape Fear Tutoring, Inc., of Wilmington, North Carolina, was selected for review based on its large size and rapid growth. We did not identify any significant program abuses by the sponsor. However, we did identify several conditions that require corrective action.

The sponsor's oversight of providers' claims was deficient. Twenty-five percent of the providers we visited claimed meals they did not serve. The sponsor's monitoring procedures were not sufficient to identify the types of deficiencies we found. The monitors announced their visits in advance and did not perform evaluations of child enrollment, attendance, and meal count data.

The sponsor did not train all providers on their duties and responsibilities. The sponsor also did not maintain the required enrollment information for children under the care of the providers. Without this information, the sponsor cannot ensure the children claimed by the providers are eligible for meal service.

**Ohio**

**New Jerusalem Church of God in Christ, Audit No. 27010-9-Ch**

We reviewed the New Jerusalem Church of God in Christ of Toledo, Ohio, as part of our nationwide review of CACFP sponsors. The sponsor met the criteria of being seriously deficient in its administration of the program and was terminated from the CACFP.

Our visits to the sponsor's provider homes showed that 5 provider addresses did not appear to exist. In some cases, provider addresses were for abandoned houses or vacant lots (see photo no. 6), and in other cases, residents at the addresses denied any association with the CACFP or the sponsor. At 21 homes, we found no one home during established serving hours despite repeated visits and telephone calls. Furthermore, we found 22 instances where the name of the provider, as documented in the sponsor's records, was not the same as the name of the resident. One month after our home visits, 80-percent of the providers that did not appear to exist submitted claims for meal reimbursements of about \$23,300, and the sponsor claimed \$1,848 in administrative costs associated with those providers.



**PHOTO NO. 6 - VACANT LOT LISTED AS ADDRESS FOR ACTIVE DAY CARE PROVIDER SPONSORED BY NEW JERUSALEM CHURCH OF GOD IN CHRIST IN OHIO.**

Seven persons, including the director of this sponsor, admitted to conspiring to illegally obtain more than \$1.1 million in CACFP funds through this sponsorship over a period of about 10 years. The defendants were charged with submitting false reimbursement claims. The claims were based on fictitious provider homes which allegedly provided meals to children in residential day care facilities. Each of

the defendants received numerous reimbursement checks, which they cashed upon receipt. They kept some of the proceeds for their own benefit and gave the remaining funds to another provider, who falsified the sponsor's records to conceal the fraud.

Nine individuals have been indicted and seven have pled guilty and were sentenced. The sentences range from 3 years' probation to almost 3 years' incarceration. They were ordered to pay restitution ranging from about \$7,000 to over \$790,000 each. Total restitution exceeded \$1.3 million.

We also found five homes that were so unsanitary as to potentially endanger the health of the children being cared for. We noted that the sponsor appeared to have lost its nonprofit status with the Internal Revenue Service in July 1994.

### **Oregon**

#### **Child Care Services, Inc., Audit No. 27010-5-SF**

We selected Child Care Services, Inc., of Roseburg, Oregon, for review based on our review of information at the FNS Regional Office and the Oregon State agency. The sponsor was found to be seriously deficient in its administration of the program and was terminated from the CACFP.

The sponsor did not perform all required monitoring visits and the visits that were performed were ineffective in ensuring provider compliance with program requirements. We attributed the deficiencies we found at providers' homes, in part, to inadequate training.

Providers did not maintain the required meal counts, menus, and attendance records, and they served meals that did not include the required meal components. We referred four providers to the State licensing agency for health or safety concerns.

The sponsor claimed unallowable, unapproved, and unsupported administrative costs totaling \$15,035. The sponsor claimed costs for more telephones, salaries, and employee medical and dental benefits than had been approved in its budget. The sponsor also ran a



referral service for providers and parents in southern Oregon, an activity requiring State approval, which the sponsor did not have.

Two of the sponsor's providers received CACFP benefits for their own children, based on their participation in the Food Stamp Program (FSP). However, it appeared the providers may have underreported their income from day care operations to the State FSP agency, making themselves appear eligible for benefits they were not entitled to.

## **Pennsylvania**

### **Children's Best Interests, Inc., Audit No. 27010-20-Hy**

Children's Best Interest, Inc., of Dover, Pennsylvania, was reviewed as part of our nationwide audit of CACFP sponsors. The sponsor was found to be seriously deficient in its administration of the program and was terminated from the CACFP.

Our unannounced visits to the providers and a review of the providers' claims for reimbursement disclosed widespread noncompliance with meal counting and service regulations and overclaims of about \$15,700 for the month under review. We also noted that some homes were not in compliance with licensing requirements governing capacity limits.

Our visits also identified one provider who was participating in the CACFP simultaneously under two sponsoring organizations. At two providers, conditions were of such severity (crowded and unsanitary) that we immediately referred the child safety concerns to Pennsylvania Department of Public Welfare officials for investigation.

The sponsor had not obtained the required sponsor audits for fiscal years 1996 and 1997 in a timely manner and did not complete all required monitoring visits for 1997. Nine facilities did not meet the definition of a "home" and were not eligible for CACFP funding.

### **CT Child Nutrition Services, Pennsylvania (Investigation only)**

An investigation was initiated based on a referral from FNS. A former sponsor official pled guilty to embezzlement, misapplication of funds, and theft totaling \$92,000 from the CACFP. She failed to reimburse

200 day care homes and misused funds to cover administrative expenses. The official used the embezzled money to cover personal expenses, such as her mortgage, and to buy equipment for a restaurant she owned. Sentencing will not take place due to the recent death of the official.

This investigation started before the initiation of Operation Kiddie Care. The results are included in this report, however, because it demonstrates the type and magnitude of the problems in the CACFP. Prior to prosecution, CT Child Nutrition Services was terminated by the State agency.

## **Tennessee**

### **Child Care Nutrition, Inc., Tennessee (Investigation only)**

An investigation was initiated based on a review by the State agency which revealed that the executive director had inflated claims for reimbursement. The former sponsor official of 69 day care homes was sentenced to serve 9 years and 2 months in prison and ordered to pay restitution of over \$127,400 after being convicted at trial on 59 counts for mail fraud, making false statements, and money laundering. The official inflated the number of children enrolled and the number of meals claimed, paid the day care homes the correct amount, and then issued a second check in the sponsor's name for the inflated amount. Our investigation, conducted jointly with the IRS and the Federal Bureau of Investigation (FBI), disclosed false claims totaling approximately \$127,000, including payments issued in the names of 15 individuals who were not program participants.

## **Utah**

### **Children Of The Future, Audit No. 27601-7-KC**

Children of the Future of Salt Lake City, Utah, was selected for review based on a complaint received by the FBI and a review of State agency records. This sponsor was found to be seriously deficient in its administration of the program and was terminated from the CACFP.

The sponsor misused Federal funds by requiring some providers to return a large portion of their reimbursement checks to the sponsor. The sponsor wrote checks to providers who no longer participated in the program and got other providers to cash the checks. The sponsor also gave some providers fictitious children's names to include on their meal claim forms and asked those providers to give the sponsor the money associated with the fictitious children.

Providers received about \$53,000 in questionable reimbursements from the sponsor but returned approximately \$3,300 of this to the sponsor after they were threatened.

Federal prosecutors charged the couple who owned the sponsorship with 117 counts of making false statements to a Government agency, and of embezzlement and misapplication of CACFP funds. One of the providers, who was working in concert with the sponsors, was arrested and charged in a 21-count Federal indictment. She was charged with making false statements to FNS on meal claim forms. She claimed meals when in fact she did not provide any. She was also involved in demanding and receiving kickbacks from providers. She collected approximately \$16,000 in provider money and handed it over to the sponsor. In return for her guilty plea, the provider will cooperate with OIG and testify against the sponsor.

A child care monitor working for the sponsor also admitted that he obtained checks and received kickbacks from child care providers. The monitor also admitted that he operated a pawn shop and that he loaned money to the providers through the pawn shop and accepted their child care checks as payments.

The couple who owned the sponsorship oversaw more than 400 day care home providers while operating a medical business in Lima, Peru. During provider visits, the sponsor did not ensure that the providers maintained a safe environment for the children enrolled in the program, and it did not emphasize the importance of following menus or meeting meal components. In fact, the sponsor discouraged providers from noting meal substitutions on the meal claim forms.

Several day care home providers lived in an apartment complex, shown in the following picture, which, in our opinion, was not safe for

children (see photo no. 7). For example, we observed a broken chain link fence laying across the sidewalk, electrical wiring hanging over an apartment entrance, and hazardous debris laying outside the apartments.

Another provider cared for children in a small trailer (see photo no. 8), where we observed broken bottles and an overflowing trash container.



**PHOTO NO. 7 - UNSAFE CONDITIONS AT A UTAH APARTMENT COMPLEX WHERE SEVERAL DAY CARE PROVIDERS OPERATED.**



**PHOTO NO. 8 - UNSAFE CONDITIONS OBSERVED AT SMALL TRAILER USED FOR DAY CARE IN UTAH.**

### **New Life For Children, Audit No. 27010-2-KC**

New Life For Children, of Salt Lake City, Utah, was selected for review based on a review of State agency records. We did not identify any significant program abuses by the sponsor. However, we did identify several conditions that require corrective action.

Problems existed with the sponsor's monitoring of providers. We questioned meal claims for 93 providers visited who exhibited poor recordkeeping and/or submitted unreasonable meal claims. The sponsor's controls over employee time sheets also needed improvement, and leases from sponsor management needed to be discontinued. We questioned \$14,125 in meals claimed for 93 of the 203 providers visited.

### **Washington**

#### **King County Family Child Care Association, Audit No. 27010-12-SF**

King County Family Child Care Association of Seattle, Washington, was selected for review based on allegations of improprieties received from an anonymous source. The sponsor was found to be seriously deficient in its administration of the program.

The director allowed an environment to exist in which two high-level employees appeared unaccountable for their activities and their adherence to program requirements. One employee was the assistant director/monitor and the other employee was a senior monitor.

Time, mileage, and monitoring reports prepared by these two individuals could not be reconciled with their required provider visits. Provider visits were recorded for days the employees were not working, and the numbers of visits recorded for some days were implausible. Mileage reports and monitoring reports sometimes listed different providers. Providers confirmed to us that the monitors were not actually making visits and were not providing program assistance. Some providers noted that the "provider" signatures on the monitoring reports were not theirs.

Because of the conflicting records and serious discrepancies noted, we questioned the salaries and travel expenses of these individuals. This amount totaled \$241,970.

We also found several situations that we believe constitute conflicts of interest. The director and one employee were both affiliated with day care homes under this sponsorship. Four members of the board of directors, who exercised oversight of the director, had homes under the director's supervision.

Additionally, the sponsor submitted claim information from providers that did not reconcile with monitoring reports, and it claimed administrative expenses unrelated to the CACFP.

**Provider of Rainbow Valley Day Care Homes, Mountlake Terrace, Washington (Investigation only)**

An investigation was initiated based on an allegation that the day care home provider submitted false claims for meals served to her own children. Our investigation disclosed that the provider illegally obtained \$4,400 in reimbursement for meals served to her own children, by underreporting her household income. She was placed on probation for 3 years and was ordered to make full restitution.

**Wisconsin**

**Social Development Commission, Audit No. 27601-15-Ch**

We selected the Social Development Commission of Milwaukee, Wisconsin, for review based on a potential connection with a sponsor operating in California. The sponsor met the criteria of being seriously deficient in its administration of the program.

Beginning in at least 1993, this sponsor accumulated an unexpended surplus of CACFP reimbursements that reached \$1.1 million. The State agency, which knew of the growing surplus, did not ensure that funds were spent in a timely manner. For the month of March 1998, the sponsor showed a \$220,545 deficit in its operating account to cover the recorded surplus. We also noted that the sponsor had not credited investment interest which had been earned on these surplus funds which amounted to over \$44,200.

We also found that the sponsor's accounting system did not ensure that revenues earned were solely used for the CACFP, and we believe it is possible that the surplus funds may have been used for nonprogram purposes.

The following table summarizes the audits and investigations reported on and in progress.



**Figure 2: Status of Audits and Investigations**

State <sup>1</sup>	Investigations in Progress	Audits Completed	Audits in Progress	Sponsors Terminated From the Program	Individuals Indicted or Named in a Criminal Information
Alabama		1			
Arizona	1	2			1
Arkansas		1			
California	8	6	3	5	19
Colorado	1		1		
Florida	2	1		1	
Idaho	1			1	1
Illinois		3			
Louisiana	2	2		1	
Maine		1			
Michigan	1			1	2
Missouri		1			
New Mexico	2	1			1
New York	2		1		1
North Carolina		1			
Ohio	2	1		1	11
Oregon		1		1	
Pennsylvania	3	1		2	1
Tennessee	3			2	3
Utah	1	2		1	4
Washington	2	1			
Wisconsin		1	1		
<b>TOTALS</b>	<b>31</b>	<b>27<sup>1</sup></b>	<b>6</b>	<b>16</b>	<b>44</b>

<sup>1</sup>Four audit surveys were also performed in Arkansas, Illinois, and Indiana but the findings did not warrant audit reports.

During Operation Kiddie Care, 16 sponsors were terminated from the CACFP, and 44 individuals were indicted or named in criminal informations for engaging in fraud or similar criminal activities. All of the 16 sponsors were private, nonprofit organizations that were in business solely to participate in the CACFP. These sponsors took advantage of the trust that the program places on them to provide oversight and maintain the integrity of the program. Because current program delivery methods depend on a high level of trust at the sponsor level, and that trust has been repeatedly violated, we believe FNS needs to seek new methods of delivering the CACFP that do not rely so completely on nonprofit sponsoring organizations. In the meantime, FNS needs to tighten the controls over these organizations to prevent and detect the types of abuses detailed in this report.

Exhibit A shows the States the terminated sponsors were operating in and the annual program funding in food and administrative funds paid to and through the terminated sponsors. Exhibit B is a summary of the status of investigations in process as of February 19, 1999. Exhibit C presents an overall summary of the audits and investigations conducted as part of Operation Kiddie Care.

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## **RECOMMENDATION NO. 1**

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Study alternative methods of delivering a meal program to children and adults in day care, specifically one that addresses the problems noted in this report at private, nonprofit organizations.

While the above study is underway and the program continues in its current form, FNS also needs to strengthen controls by implementing the recommendations provided at the end of Finding No. 2.

## **FNS Response**

In its written response to the draft report, dated July 27, 1999, FNS stated, "In the Fall 1999, a task force will be assembled to study alternative methods of delivering a meal program."

## **OIG Position**

In order to reach management decision, FNS needs to provide details of how, when, and by whom this study will be conducted. As stated in this audit report, FNS has been studying how to improve the integrity in the CACFP since March 1995. Specific timeframes and objectives need to be established to complete this study.

We urge FNS to give high priority to completing the study and to emphasize the most serious problems we have encountered -- disreputable private nonprofit sponsors, the need for an alternative method of paying sponsors for their administrative costs, and the need for bonding of key sponsor officials (see also recommendations 2h and 2k).

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### **FINDING NO. 2**

#### **FNS HAS NOT YET CORRECTED EXISTING PROBLEMS: IMMEDIATE CONTROLS ARE NEEDED DURING PROGRAM REDESIGN**

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Over the past 4 years, FNS has been provided information which showed that significant problems exist in the CACFP. Until recently, FNS has generally taken the position that the problems were not of a magnitude to warrant aggressive changes. In responding to its own task force's call in 1995 for corrective action, FNS deferred implementation of any change

until the end of the year 2000. We believe that the conditions we found require immediate corrective actions.

Since March of 1995, OIG has issued two Nationwide reports and four national management alerts reporting significant problems in the CACFP. An FNS task force also issued a report that made 33 recommendations to improve program integrity.

**a. OIG Reported Problems in the Program in March 1995**

In March 1995, OIG issued an audit report<sup>2</sup> that detailed a review of a randomly selected sample of sponsors and providers in the States of California, Georgia, Kansas, Minnesota, and Texas. At that time, these States disbursed to sponsors of day care homes about \$122 million for meals served and about \$17.6 million for sponsor administrative costs annually.

Based on the various conditions noted at the sample sponsors and day care homes, OIG statistically estimated that within the five States:

- 3,713 homes claimed meals totaling over \$6 million, during the period October 1992 through April 1993, for absent and/or nonexistent children,
- 22,246 homes did not maintain current meal count and/or menu records for meals served, resulting in unsupported meal claims totaling over \$2.5 million,
- 160 sponsors did not perform all required monitoring visits to homes, and
- 201 sponsors did not require home providers to attend program and child care training.

The audit concluded that management controls over program operations were not well designed to prevent or detect inflated and unsupported meal claims. Only 6 of the 38 sponsors reviewed routinely contacted parents to verify child attendance times and claimed meals. Only 16 of the 38 required that care providers attend training.

The audit also concluded that State agency and FNS oversight reviews did not focus on the primary management controls at the sponsor and the day care homes. State agency administrative

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<sup>2</sup>Audit Report No. 27600-6-At, Food and Consumer Service, Child and Adult Care Food Program, Day Care Homes-Nationwide, issued March 31, 1995.

reviews of sponsors and homes generally did not include sufficient tests to identify inflated and unsupported meal claims and assess the adequacy of sponsors' monitoring of homes. Most FNS management evaluations did not include sponsor or home visits.

The audit recommended that FNS establish required review coverage areas for both State agencies and sponsors. It also recommended that FNS:

- (1) explore alternative systems of administrative cost reimbursement so the reimbursements are not directly based on the number of homes and do not create a financial disincentive to effective compliance;
- (2) consider emphasizing monthly budgeting and strengthening sponsor eligibility requirements;
- (3) strengthen regulations to require that all participating child care providers receive a specific minimum number of hours in program and child care training each year;
- (4) require that sponsors and State agencies verify at least annually that participating homes receive the prescribed training;
- (5) require that State agency administrative reviews of sponsors and homes include steps to identify recordkeeping deficiencies and inflated meal claims, and steps to assess the adequacy of sponsor monitoring of day care homes (reviews should include unannounced home visits and parent contacts); and
- (6) modify FNS management evaluation coverage to include specific steps to assess the effectiveness of State and sponsor monitoring of homes (audits, homes visits, administrative and other reviews, and meal claim edits).

The full text of the report was provided to FNS with the official draft report.

In response to this report, FNS proposed that its own CACFP task force would begin "to improve program integrity, streamline the operations of the CACFP in an attempt to make the program easier to operate at the State and local levels, and maintain a program which is fully open to all well-managed sponsoring organizations and the children they serve."

**b. The FNS Task Force Acknowledged Problems in July 1995 but Recommendations Were Deferred Until the End of Year 2000**

The CACFP task force was a collaborative State agency and FNS effort involving 14 individuals from 7 State agencies and 7 FNS regional offices. It convened in March 1995, and in July 1995 it made 33 recommendations to change the CACFP in the areas of program approval criteria, training and operations, and sponsor oversight. The task force also began developing program operational material for the family day care home program.

The task force made recommendations to strengthen the CACFP. In our opinion, if these recommendations had been implemented, many sponsor abuses would have been prevented or detected.

Among other things, the Task Force recommended that FNS:

- (1) establish standards for the approval of new sponsoring organizations, and standards for renewal of current sponsoring organizations,
- (2) strengthen the regulations for terminating sponsors and allow the States some flexibility in selecting sponsors for review, and
- (3) provide performance standards and guidance for reviewing sponsors' management plans, for evaluating the composition of sponsors' boards of directors, for setting salaries, and for ensuring that sponsors are competent and that they receive training.

The full text of the report was provided to FNS with the official draft report.

In response to the Task Force report, on May 18, 1997, about 2 years after the Task Force made its recommendations, FNS issued a Management Improvement Guide "to assist State agencies, sponsoring organizations, and providers in evaluating whether they are administering a quality child care feeding program." In the transmittal letter transmitting this guide to the State agencies, FNS stated that "State agencies, sponsors and providers may use these materials for self-evaluation, performance assessment and monitoring."

Even after receiving a strong warning about problems in the CACFP and recommendations to correct these problems from its own Task Force, FNS only issued this optional "self-evaluation" guidance to State agencies and sponsors.

In response to Task Force recommendations to establish sponsor standards and to strengthen the CACFP regulations, FNS did not initiate corrective action immediately but arrived at a long-range plan to address the task forces' concerns and recommendations. Final implementation of corrective actions in the long-range plan are not anticipated until the fourth quarter of fiscal year 2000, about 5 years after the recommendations were made.

Most of the areas addressed by the FNS task force in 1995 turned out to be significant problem areas found during our audits and investigations of individual sponsors in Operation Kiddie Care. If the task force standards for approving and reviewing sponsors had been implemented and enforced, many of the issues involving the problem sponsors we reviewed would have been resolved.

**c. Operation Kiddie Care (Interim Report issued April 1998)**

In April 1998, the Inspector General issued an interim report on the results of OIG's audits and investigations of CACFP sponsors, to alert FNS to significant problems in the program.

Operation Kiddie Care found significant weaknesses in program delivery. CACFP sponsors were found to be submitting false claims on a large scale. We reported that "for this \$1.6 billion-a-year program that feeds an estimated 2.4 million children annually, the temptation to cheat was too great and the controls to prevent cheating were too weak."

Serious program irregularities were found at 33 sponsors; 26 investigations for program fraud were initiated; and 10 sponsors were terminated from the CACFP. These 10 sponsors were receiving \$23 million annually in food and administrative funds.

The Operation Kiddie Care report recommended that fundamental program changes be considered as part of the CACFP reauthorization process. Suggestions included:

- (1) Determining if alternate methods of reimbursing sponsors for administrative costs should be considered. The current method of paying sponsors based on the number of homes they administer creates a disincentive to proper program management.
- (2) Restricting providers in their ability to change sponsorships. Providers can now readily change to sponsors that do not enforce the program requirements.
- (3) Seeking legislation to clarify reimbursement of administrative costs to sponsors of day care centers. The law should be made explicit for sponsors of day care centers. The current reimbursement methodology of allowing sponsors to take a high percentage of the food reimbursement creates an opportunity for sponsors to abuse the program.
- (4) Clarifying legislation to terminate sponsors from program participation.

The full text of the report was provided to FNS with the official draft report.



After we issued this report FNS reconvened the 1995 "Integrity" CACFP Task Force. Based on its first meeting in February 1999, the Task Force set forth proposed areas for followup to improve the management of the CACFP.

**d. FNS has not Acted on Management Alerts**

During the course of this Presidential Initiative, we have issued a series of management alerts notifying the FNS National Office of deficiencies which should have been corrected as soon as possible. As part of the audit process, we issue management alerts to notify agency officials of conditions we have found which warrant immediate attention. Agency managers are required by Departmental Regulations (DR 1720-1) to take prompt action on potential problems or significant weaknesses when reported to the agency before an audit report is issued.

Although FNS would usually respond that it would act on our recommendations, we found during our December 1998 work at the FNS National Office, that corrective actions were generally not taken. A summary of these management alerts are presented here. The three management alerts which, in our opinion, need to be addressed as part of this audit report (1, 2, and 3 below) are presented as findings later in this report.

1. Management Alert Issued on June 4, 1997

In this management alert, we notified FNS that we found that many child care providers claiming reimbursement for meals served to their own children, based on their participation in the Food Stamp Program or other welfare programs, had underreported their child care income to the State Food Stamp agency. By not reporting their income, these providers may have received undeserved Food Stamp and CACFP benefits.

On July 21, 1997, FNS informed us that they would act on this problem. As of December 1998, about 18 months later, no actions had been taken.

2. Management Alert Issued on December 1, 1997

In this management alert, we notified FNS that some States allowed sponsors of independent day care centers to retain a portion of the centers' food reimbursement as a means of recovering the cost of administering the centers' participation in the CACFP. FNS permitted this practice but offered no guidance on the amount of money that may be taken. In our opinion, this practice was unfair to centers, reduced funds intended to feed children, and created an environment that encouraged fraud and abuse in the CACFP. In the management alert we recommended that FNS establish a realistic rate for sponsors of day care centers, and to notify all centers that they did not have to enter into these arrangements with sponsors.

In its response to this management alert, dated December 19, 1997, FNS disagreed with setting a rate for sponsors of centers but stated that they would act on the other recommendations. On April 20, 1998, about 5 months after the management alert was issued, FNS notified its regions that OIG had reported "what they perceive to be a problem in the CACFP" and instructed their regions to "request that all State agencies which administer the CACFP advise sponsored centers that they have the option of becoming an independent center." The FNS National Office also stated that "we are considering a policy memorandum to address OIG concerns in the area of administrative costs."

As of December 1998, 1 year after the management alert was issued, except for requesting that all States notify their sponsored child care centers that they had the option to become independent centers which contract directly with the State agency, no further action was taken to correct this serious deficiency. FNS did not address the problem of administrative costs paid to sponsors of day care centers.

3. Management Alert Issued on July 24, 1998

In this management alert, we notified FNS that California was attempting to recover overpayments to sponsors by using a method which penalized providers who were not responsible for the overpayments, and which may directly harm children in their care. We found that this situation may have had national implications and needed immediate corrective action.

On August 13, 1998, FNS stated that they would issue guidance to all of their regional offices within 60 days on appropriate recovery procedures.

As of December 1998, 5 months after the management alert was issued, FNS had not acted on this alert.

4. Management Alert Issued on September 16, 1998

In this management alert, we notified FNS that the agency needed to implement regulations to prohibit the commingling of administrative funds and provider food funds and prohibit sponsors from commingling funds between the CACFP accounts and other funds of organizations affiliated with the sponsor. These recommendations were made because we found that one of the largest sponsors in the country was shifting funds between the various CACFP and non-CACFP accounts to cover the fact the it was running a deficit in the CACFP program, which indicates a serious deficiency which if not corrected could ultimately result in providers not receiving their food reimbursements.

On October 13, 1998, FNS stated that "we appreciate the intent of the recommendations, however we believe the current CACFP regulations provide sufficient authority to address the improper use of administrative and meal service (provider) funds."

Shifting money between program and nonprogram accounts is a method used by sponsors to hide the fact that they are not paying the providers and the children they are trying to feed (see Audit Report 27010-11-SF).

**e. As of February 1999, Operation Kiddie Care Continued To Disclose More Cases of Program Abuse**

After the release of the Interim Operation Kiddie Care Report, OIG continued to find widespread abuse and fraud in this program. As of February 19, 1999, we had found the following:

- ! Whereas 33 sponsors had been identified in April 1998 with serious program irregularities, there are now 37; whereas 26 investigations had been initiated for program fraud, there are now 31.
- ! The number of sponsors terminated from the CACFP has also risen. By April 1998, 10 sponsors receiving \$23 million annually in food and administrative funds had been terminated; to date, 16 sponsors receiving approximately \$34.6 million annually have been terminated.
- ! The number of individuals who had been indicted or named in criminal information documents has risen from 13 in April 1998 to 44. The number of individuals who pled guilty or were convicted has risen from 9 to 28; and the number who were sentenced for illegal activities has risen from 4 to 26.

Operation Kiddie Care has shown that the CACFP is highly susceptible to fraud, waste, and abuse. The recommendations made below address the problems we found during our audits, including lack of standards for approving and renewing sponsorships. Many of these recommendations were made previously in the reports we discussed, but FNS did not take the opportunity to act on them.

Recommendation number 2h is a restatement of a recommendation made in the 1995 OIG audit report. At that time, OIG accepted FNS' management decision not to explore alternative systems of administrative cost reimbursement for sponsors of day care homes. We are restating this recommendation in this report because Operation Kiddie Care has shown that this method of paying administrative costs for sponsors of day care homes is a disincentive to proper program administration and needs to be changed.

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## **RECOMMENDATION NO. 2a**

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Revise regulations to include standards for approving and renewing sponsors. Sponsors should have business experience, adequate management plans and budgets, demonstrate financial capability and a standard of ethics, and undergo a criminal background check.

### **FNS Response**

In its written response to the draft report, dated July 27, 1999, FNS stated, "A proposed integrity rule to be published in the Fall 1999."

### **OIG Position**

In order to reach management decision, please provide specific details from the published proposed rule which address this recommendation and the proposed issuance date for the final rule.

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## **RECOMMENDATION NO. 2b**

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Revise regulations to include standards for terminating sponsors. Sponsors should face termination for engaging in inappropriate business practices, falsifying program information, and concealing a criminal background.

### **FNS Response**

In its written response to the draft report, dated July 27, 1999, FNS stated, "A proposed integrity rule to be published in the Fall 1999."

### **OIG Position**

In order to reach management decision, please provide specific details from the published proposed rule which address this recommendation and the proposed issuance date for the final rule.

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## **RECOMMENDATION NO. 2c**

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Provide guidance to State agencies on the composition of governing boards of sponsors, and clarify the required oversight and independence of these boards.

### **FNS Response**

In its written response to the draft report, dated July 27, 1999, FNS stated

Addressed in the Agency's Management Improvement Guidance and in a management assessment guide (attached) which was distributed to SAs in May 1999. Developing a Board of Directors Fact Sheet which is to be completed and distributed in September 1999.

### **OIG Position**

The Management Improvement Guidance is an optional, self-assessment guide for State agencies, sponsors and providers and will not remedy the causes of the problems disclosed in this finding. In order to reach management decision, please provide a specific plan of action to be taken on this recommendation and the proposed completion date.

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## **RECOMMENDATION NO. 2d**

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Provide State agencies guidance on how to set administrative salary guidelines for employees of CACFP sponsors that are consistent with local salary structures.

### **FNS Response**

In its written response to the draft report, dated July 27, 1999, FNS stated, "FNS will issue memorandum to SAs in the Fall 1999."

### **OIG Position**

In order to reach management decision, please provide specific details of the directions to be provided in the memorandum to the State agencies in the Fall of 1999.

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## **RECOMMENDATION NO. 2e**

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Allow State agencies to devote up to 20 percent of the required review time within a review cycle to additional reviews of new and problem sponsors. (For example, within a review cycle, if a State uses 100 staff days to accomplish CACFP reviews, it may shift 20 of these days to problem or new sponsors by diminishing review days used for other sponsors.)

### **FNS Response**

In its written response to the draft report, dated July 27, 1999, FNS stated, "A proposed integrity rule to be published in the Fall 1999."

### **OIG Position**

In order to reach management decision, please provide specific details from the published proposed rule which address this recommendation and the proposed issuance date for the final rule

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## **RECOMMENDATION NO. 2f**

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Expand the authorized actions against "seriously deficient" sponsors: (1) to allow for the immediate termination of a sponsor charged by another government agency (Federal, State, or local) with having placed the health or safety of a child in jeopardy; (2) to include sponsors whose agreement lapses prior to termination; and (3) to require automatic termination or suspension of a sponsor for fraud.

### **FNS Response**

In its written response to the draft report, dated July 27, 1999, FNS stated, "A proposed integrity rule to be published in the Fall 1999."

### **OIG Position**

In order to reach management decision, please provide specific details from the published proposed rule which address this recommendation and the proposed issuance date for the final rule.

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## **RECOMMENDATION NO. 2g**

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Establish required review coverage and standardized reporting for sponsor monitoring of providers to include: (1) assessing whether enrollment, meal count, and menu records are current and complete, and (2) reconciling observed attendance with enrollment data and with the subsequent meal count that is claimed.



### **FNS Response**

In its written response to the draft report, dated July 27, 1999, FNS stated

A proposed integrity rule to be published in the Fall 1999. Addressed in the CACFP management standards for family day care home sponsoring organizations which were published and distributed to SAs in May 1997.

### **OIG Position**

In order to reach management decision, please provide specific details from the published proposed rule which address this recommendation and the proposed issuance date for the final rule.

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## **RECOMMENDATION NO. 2h**

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Establish an alternative system of administrative cost reimbursement so that it is not directly based on day care home numbers and do not create a financial disincentive to compliance enforcement.

### **FNS Response**

In its written response to the draft report, dated July 27, 1999, FNS stated, "In the Fall 1999, a task force will be assembled to study alternative methods of delivering a meal program."

### **OIG Position**

The OIG audit of the CACFP completed in March 1995 recommended that FNS explore alternative systems of administrative cost reimbursement so that reimbursements are not directly based on the number of homes; thus eliminating the financial disincentive to effective compliance.

Both in the 1995 audit and in our current 1999 audit, we found that because sponsors were paid administrative costs based on the number of homes they sponsored, the sponsors were actually competing against one another for homes. The more homes a sponsor had, the more administrative costs they could claim.

This competition for homes, and the ease by which homes can switch sponsors, creates a situation where sponsors are reluctant to enforce the program requirements at the provider level. Sponsors told us that the competition between sponsors created by this system has made it difficult for the sponsors to administer the program. This is a basic flaw in the design of the CACFP and needs to be corrected as soon as possible. We do not believe that it needs further study.

In order to reach management decision, please provide a specific plan of action to be taken on this recommendation and the proposed completion date.

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## **RECOMMENDATION NO. 2i**

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Strengthen the provider regulations to require that all participating providers must receive a specified minimum number of hours in program training each year and require State agencies to verify that providers received the prescribed training.

### **FNS Response**

In its written response to the draft report, dated July 27, 1999, FNS stated, "A proposed integrity rule to be published in the Fall 1999."

### **OIG Position**

In order to meet management decision, please provide specific details from the published proposed rule which address this recommendation and the proposed issuance date for the final rule.

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## **RECOMMENDATION NO. 2j**

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Require that State agency administrative reviews of sponsors and day care homes include steps to identify recordkeeping deficiencies and inflated meal claims, and to assess the adequacy of sponsor monitoring of the homes. Reviews should include unannounced day care home visits and parent contacts.

### **FNS Response**

In its written response to the draft report, dated July 27, 1999, FNS stated

A proposed integrity rule to be published in the Fall 1999. Also, this was addressed in the CACFP management standards for family day care home sponsoring organizations which were published and distributed to SAs in May 1997.

### **OIG Position**

In order to reach management decision, please provide specific details from the published proposed rule which address this recommendation and the proposed issuance date for the final rule.

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## **RECOMMENDATION NO. 2k**

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Require owners and officers to be bonded so that program funds lost through their inappropriate actions will be restored to the program. If bonding requires a change in the current legislation, FNS should work with OMB to propose this legislative change.

## **FNS Response**

In its written response to the draft report, dated July 27, 1999, FNS stated

Office of Management and Budget (OMB) Circular A-102, Attachment B, prohibits Federal agencies from promulgating bonding requirements except when required by law. This issue will be analyzed as part of the larger study of Program re-design in the Fall 1999.

## **OIG Position**

We revised this recommendation to state that if legislation is required to implement a bonding requirement, FNS should work with OMB to implement such legislation. In order to prevent disreputable individuals from participating in the CACFP and to facilitate collecting identified overpayments, FNS should implement a bonding requirement of key sponsor officials. This good business practice has already been implemented by Texas and is being proposed by California. We see no reason to study this issue further.

In order to reach management decision, please provide a specific plan of action to be taken on this recommendation and the proposed completion date.

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### **FINDING NO. 3**

#### **EXCESSIVE ALLOWANCE FOR ADMINISTRATIVE COSTS OF DAY CARE CENTERS IS AN INCENTIVE FOR ABUSE**

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Some States allow sponsors of independent child care centers to retain a portion of the centers' food reimbursements as a means of recovering the cost of administering the centers' participation in the CACFP. FNS has permitted this practice but has offered no guidance on the amount of money that may be taken. In our opinion, this situation is unfair to centers, reduces funds intended to feed children, may not be provided for in the current CACFP regulations, and creates an environment that has encouraged fraud and abuse in the CACFP.

The Code of Federal Regulations 7 CFR 226, paragraph 226.2 (Definitions), states that "Child care centers may participate in the

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Program as independent centers or under the auspices of a sponsoring organization." These regulations are silent on how much, if any, can be paid to the sponsors for their costs of administering the CACFP to centers.

FNS Instruction 796-2, Rev. 2, Financial Management - Child and Adult Care Food Program, paragraph IX F 2, states that "Sponsors of these centers may vary the amount of reimbursement paid to sponsoring facilities up to the maximum allowed or retain a portion of the rates for their administrative costs in accordance with the management plan approved by the State agency." We found that this obscure reference was interpreted differently by different States and we could find no other legal or regulatory basis for this practice.

At least seven States allow sponsors to take a percentage of the food reimbursement intended for centers to cover the sponsors' administrative costs. For example, California allowed sponsors of centers to take up to 30 percent of the food reimbursement (as a result of our disclosures that many of these sponsors were defrauding the program, California dropped the allowed percentage to 15 percent effective October 1, 1998); Mississippi allows 10 to 20 percent; Alabama, 25 percent; Florida, 15 to 20 percent; Tennessee, 30 percent; and New York, 30 percent. Some States do not allow sponsors to take any of the food money for administrative costs.

The large amount of funds being retained by sponsors through this practice encourages abuse of the program. These funds must be used for program purposes. In California, for example, all six sponsors we audited that retained 30 percent of their centers' food reimbursements were found to be seriously deficient in program administration; five of the six were investigated (and in three of the five cases, nine individuals were sentenced) for program fraud; and, as of the date of this report, three of the six were terminated from the program.

The amount of funds retained by sponsors also has no correlation with actual costs of administering the centers. For example, one sponsor's budget, approved by the State, allowed \$289,901 for its administration of 355 homes and \$301,321 for its administration of 38 centers. On average, the sponsor received about \$68 per month for each day care home provider and \$661 per month for each center. Another sponsor's budget allowed for \$1,112 per month for administrative expenses for each center. Neither of these sponsors

had justified to the State agency why they needed so much more to administer the CACFP to child care centers versus the amounts budgeted for the day care homes.

We could find no reason why sponsors should retain these large amounts of food reimbursement. The time needed to process the centers' claims for reimbursement may be slightly longer because centers have more children in attendance but the required time to administer all other program requirements (training, monitoring, etc.) is the same for both types of day care facilities.

In both of the cases cited above, we found the sponsors to be diverting to unauthorized uses the funds made available through the 30-percent calculation.

Because of the amount of work and adverse conditions we found with sponsors retaining 30 percent of centers' food money, California decided that effective October 1, 1998, they would reduce the maximum allowable retention to 15 percent. As can be seen from the above example, 15 percent may still be too high, but we estimate that approximately in California \$568,000 annually will now be available to feed children because of this change.

On December 1, 1997, we issued a management alert notifying the FNS Administrator of this situation and recommended that FNS establish a realistic rate that sponsors can retain for administering the program to the centers. The rate should more closely equal what a sponsor is paid to administer the program for day care providers.

FNS responded to this management alert on December 19, 1997, by stating:

We do not believe that a National standard for administrative costs allowed could reasonably be applied to all sponsoring organizations. In addition, we believe implementing such a rate may be counterproductive. Establishing a rate to be used for all sponsoring organizations may actually increase the amount of administrative costs claimed since some sponsoring organizations currently take no administrative reimbursement for oversight of their centers, and in others, only minimal administrative reimbursement is claimed. By identifying permissible maximum rates of administrative reimbursement we might be encouraging such sponsors to begin or increase charges.

The sponsors whom FNS believes are taking no food reimbursement usually either prepare the meals for the centers or have complete financial control over the centers, so any funds not spent on food would be retained by the sponsor anyway. Providing direction to sponsors of independent centers would not in any way effect these sponsors.

In addition, FNS needs to determine if it is legal for sponsors to obtain reimbursement for administrative costs by retaining funds that are owed to centers for providing food to children. If the practice is legal, FNS needs to establish reasonable rates. All centers need to be notified that by participating with the State agency, they can save the administrative cost retained by the sponsor.

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### **RECOMMENDATION NO. 3a**

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Determine from the OGC whether it is legal for sponsors to recover administrative costs by retaining a portion of the funds earned by centers providing food to children. If this practice is determined to be legal, and until the legal determination is made, implement Recommendations 3b, 3c, and 3d.

#### **FNS Response**

In its written response to the draft report, dated July 27, 1999, FNS stated, "FNS will seek legal opinion from the Office of General Counsel by the Summer 1999."

#### **OIG Position**

We accept management decision on this recommendation.

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### **RECOMMENDATION NO. 3b**

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Notify all child care centers that participate under sponsors that they have the option to participate directly with the State agency.

## **FNS Response**

In its written response to the draft report, dated July 27, 1999, FNS stated

Completed. FNS issued guidance on April 20, 1998 to SAs instructing them to inform centers that they may participate as independent centers (as opposed to being sponsored) under a direct agreement with the SA. The were also informed to let centers know that if they chose to participate under a sponsoring organization, a portion of their food reimbursement may be retained by the sponsoring organization to cover administrative costs. FNS will have training from September 1999 to January 2000.

## **OIG Position**

We accept management decision on this recommendation.

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## **RECOMMENDATION NO. 3c**

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Inform centers that if they choose to participate under the auspices of a sponsoring organization, the sponsoring organization may retain a portion of their food reimbursement to cover their administrative costs.

## **FNS Response**

In its written response to the draft report, dated July 27, 1999, FNS stated

Completed. FNS issued guidance on April 20, 1998 to SAs instructing them to inform centers that they may participate as independent centers (as opposed to being sponsored) under a direct agreement with the SA. The were also informed to let centers know that if they chose to participate under a sponsoring organization, a portion of their food reimbursement may be retained by the sponsoring organization to cover administrative

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costs. FNS will have training from September 1999 to January 2000.

### **OIG Position**

We accept management decision on this recommendation.

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## **RECOMMENDATION NO. 3d**

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Establish a realistic rate that sponsors can retain for administering the program to the centers. The rate should more closely equal what a sponsor is paid to administer the program for day care providers.

### **FNS Response**

In its written response to the draft report, dated July 27, 1999, FNS stated

A proposed integrity rule, to be published in the Fall 1999, incorporates performance standards which address allowable cost.

### **OIG Position**

As shown in the results of this audit, this is one of the most significant causes of fraud and mismanagement in the CACFP; the retention of food reimbursement by sponsors of child care centers for their administrative costs.

In order to reach management decision, please provide specific details from the published proposed rule which address this recommendation and the proposed issuance date for the final rule.

## **II. SPONSORS AND STATES NEED FNS WRITTEN GUIDANCE FOR ADMINISTRATIVE ACTIVITIES**

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### **FINDING NO. 4**

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In addition to the aforementioned cases of fraud and program abuse, we found that sponsors and State agencies alike generally did not understand all that was required of the sponsors to administer the program. In our opinion, this is a cause of some of the serious deficiencies we found at the sponsors, and an overall weakness in the program. While not all of the sponsors we audited were committing program fraud, most of them were submitting questionable claims in one form or another.

FNS needs to develop program administration regulations and issue a sponsors' handbook for administrative management of the CACFP. Currently, the guidance that exists is decentralized. It exists in a host of program regulations, FNS instructions, and Office of Management and Budget (OMB) Circulars. Included among the directives that control the program are 7 CFR, parts 226 and 3015; OMB Circulars A-87 and A-122; FNS Instruction 796-2, Financial Management - Child and Adult Care Food Program; and the National School Lunch Act (Public Law 102-518).

Most of the problem sponsors we found during Operation Kiddie Care were in business solely because of the CACFP. They were usually small organizations with staffs consisting of a few officers, monitors, and administrative support personnel. Most of these sponsors were not following the ambiguous, decentralized Federal and State directives.

Although FNS has developed very helpful CACFP program handbooks on nutrition and monitoring, it offers no similar handbook on administrative management. Sponsors need clear direction on the eligibility of administrative costs, such as expenses for travel, leased vehicles, employee benefits, office space, salary allocation, and training. Sponsors also need direction on the degree to which outside employment by key employees is compatible with adequate management of the program.

Following are examples of some of the administrative cost areas where we found the regulations and guidance to be inadequate, ambiguous or nonexistent.

### **Outside Employment**

We could find no specific Federal regulations or guidance concerning the outside employment of key sponsor employees. At best, these regulations refer only to adequate staffing. The regulations state, "Each institution shall provide adequate supervisory and operational personnel for management and monitoring of the CACFP."<sup>3</sup>

Some States offer no clearer guidance. California, for example, requires the sponsor to maintain an adequate staff to operate a quality CACFP.<sup>4</sup> This State also includes in its agreement with the sponsor the requirement that the sponsor administer the CACFP from an ongoing office site staffed by permanent administrative personnel.<sup>5</sup> Neither Federal nor California State directives identify when outside employment by sponsor employees may interfere with "adequate" supervision.

We concluded that outside employment did interfere with the operations of some sponsors.

- At one sponsor, two of the three key employees had outside employment or school responsibilities. The third employee was also away from the office nearly 2 weeks out of every month while conducting visits to homes and centers. For some periods, no one was present in the office during normal child-care hours.

The deputy director, the highest ranking official of the sponsor, worked full time at another government job. Based on her schedule, the deputy director could only work 10 percent of her normal work hours on the CACFP (unless she took leave from her non-CACFP job). However, she charged approximately 136 hours per month to the CACFP. The deputy director stated that

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<sup>3</sup>7 CFR 226.15(d), dated January 1, 1995.

<sup>4</sup>California Department of Education Day Care Home Sponsor Manual, Section 200, dated September 1995 (revised May 1997).

<sup>5</sup>California Department of Education Form: CNFDD 2050 (revised June 1995).

she worked most of these 136 hours during weekends and in the evenings after her full-time job.

- For another sponsor, three key employees were engaged in nonprogram activities at the same location used to carry out CACFP functions. The executive director and the accountant operated a bail bonds business from the sponsor's offices, and only a small sign on the side of the building indicated it was in fact a CACFP sponsor office.

Also, while carrying out CACFP functions, sponsor employees presented themselves as income tax consultants and promoted this and other services to providers and others through the sponsor's publications.

- The executive director of a California sponsor was paid a salary from the California CACFP program and had use of a vehicle, also paid for by the California CACFP program, while residing and working full-time for other enterprises in Wisconsin. We found no evidence that the executive director was actively participating in the day-to-day operations of the California sponsor.
- In Florida, the executive director and his wife (a former employee) were paid a salary from the Florida CACFP program while residing in North Carolina. The program also paid for the executive director's travel expenses incurred between North Carolina and Florida. At this time, we do not know if the executive director had another job in North Carolina. However, we feel that it is unreasonable to operate a sponsorship in one state, but reside in another.

FNS and State program officials have contended that current regulations do not preclude sponsor officials from holding other full-time jobs while also drawing a full-time salary from the CACFP.

In our opinion, clear program guidance needs to be provided to States and sponsors concerning the issue of outside employment, reasonable workhours, and staffing the sponsors' offices to make sure that sponsors adequately service the providers.

## **Government-Funded Vehicles**

FNS also needs to give clear direction on the use of Government-funded vehicles in the CACFP. In most cases we reviewed, sponsors who leased vehicles and claimed them in the CACFP, put the vehicles at the disposal of high-level sponsor employees, often for nonprogram purposes. The monitors who actually serviced the providers and would have the greatest need for leased vehicles did not use them.

The requirement that best addresses this situation is OMB Circular A-122, "Cost Principles for Nonprofit Organizations." This rule states that a cost is allocable to a Federal award if it is incurred specifically for the award.

For one sponsor, CACFP funds were used to pay for leased vehicles for both the program director and the assistant program director (a husband and wife team). The program director informed us that the vehicles in question were "perks." She stated that during the scope of our audit, the vehicles were exclusively used by the director and assistant director and kept at their personal residences.

The program director added that although she knew she could prorate vehicle expenses between personal and business expenses, she elected not to do this because the vehicles were considered employee benefits (see the following section on employee benefits). She stated that the cars were readily available for monitoring visits, but she could not recall an occasion within the past 2 years when they were so used.

Since the vehicles were used exclusively for personal purposes and not program purposes, we questioned almost \$15,000 for all expenses associated with the vehicles.

State representatives confirmed that vehicles leased by a sponsor should only be used for program purposes. They pointed out that the lease was disclosed in the budget even though in the above case, the budgeted items used for nonprogram purposes are not authorized expenditures.

We also questioned the total lease payments for a vehicle used by the executive director of a sponsor located in California. In a meeting with the executive director, we confirmed that the vehicle was physically located in Wisconsin. Since the sponsor was making the payments for the vehicle, and the use of a vehicle was authorized by the State, the vehicle should have been used for program purposes in California.

### **Travel Expenses**

The claiming of travel expenses is neither consistent nor reasonable. Some States require sponsors to follow State travel policy; other States allow sponsors to claim whatever they feel they are entitled to.

In California, sponsors are allowed to travel within the State without following any policies. They are only required to ensure that the travel and expenditures are necessary and reasonable. However, there are no regulations that provide guidance as to what constitutes necessary and reasonable expenditures.

For example, the program director of a California sponsor attended many roundtable meetings throughout the year. These roundtable meetings were held in California every other month. Usually, only the director and the program administrator attended the roundtable meetings. However, for one roundtable meeting held in San Francisco, the sponsor sent five employees without obtaining approval. On another occasion in Atlanta, the program director along with the program administrator attended a national conference. Besides the fact that only one person was allowed by the State agency to attend this out-of-state conference, the two employees spent \$120 on dinner one evening. This was considered allowable because there are no regulations on what is reasonable and no limits on what can be claimed.

State agency personnel informed us that the travel policy the sponsor was following--claiming whatever it felt was reasonable and necessary--was a statewide policy. However, we could find no written State document that espoused this policy. The State personnel added that they had received no instruction from FNS telling them what travel policies should be followed. Since this is 100 percent federal funds, it costs the State agency nothing.

We believe that FNS should ensure continuity and integrity in the program by requiring sponsors to follow prescribed travel policies.

**Benefits**

The payment of benefit packages for sponsor executives varied considerably. We found States that allowed sponsors to claim 100-percent of CACFP funding for their retirement and benefit packages, while other States only approved limited retirement packages through which the employee contributed a percentage of the benefit.

OMB Circular A-122, "Cost Principles for Nonprofit Organizations," states that "costs of the organization's pension plan which are incurred in accordance with the established policies of the organization are allowable, provided such policies meet the test of reasonableness."

During our review of sponsors in one State, we found that the benefits provided by one sponsor to its key employees were excessive when compared to the benefits provided by seven other sponsors. The State agency provided us with the following schedule:

**Figure 5: State Data Showing Disproportion of Employee Benefits Among Sponsors**

Sponsor No.	Budgeted No. of Homes	Budgeted Admin. Labor & Employer Taxes	Budgeted Employee Benefits	Benefits % of Labor/Taxes
1	1,050	339,464	91,200	27
2	1,050	369,984	42,852	12
3	1,600	521,564	110,940	21
4	430	226,147	16,764	7
5	325	182,291	16,808	9
6	300	166,370	5,796	3
7	284	124,349	6,782	5
8	198	90,674	13,483	15

As the schedule shows, sponsor no. 1, with 1,050 homes under its sponsorship, paid out employee benefits that totaled over a quarter of the cost of its labor and payroll taxes. The sponsor with the most homes under its sponsorship, 1,600, paid out 21 percent of the same costs, while the sponsor with the same number of homes as sponsor no. 1 paid out employee benefits totaling 12 percent of these costs.

To ensure continuity and integrity in the program, FNS should require sponsors to develop consistent employee benefit packages.

### **Training**

Federal regulations for the CACFP state that prior to beginning program operations, the staffs of all child care and adult day care facilities must be trained in program duties. After this initial training, sponsors are required to provide training sessions not less frequently than annually.<sup>6</sup>

In several of our reviews we found variances in the sponsor's interpretation of what constitutes annual training. Some sponsors have noted that although current regulations require sponsors to offer annual training, they do not require providers to actually attend it. We found that while some sponsors presented as many as four training sessions a year, in locations convenient to the providers, other sponsors presented their training through mail courses and newsletters. In these last cases, little effort was made to accommodate provider questions.

We also found training conferences whose benefits appeared questionable in light of the probable costs to the program. One sponsor, who used the Los Angeles Arboretum for its training conference, announced the conference as an "educational festival." We learned that the training session consisted mainly of vendor booths selling children's products and entertainment provided by local child musicians, dancers, and martial arts demonstrators. The session's master of ceremonies was Mr. Happy Bo Bappy the Clown.

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<sup>6</sup>7 CFR 226.16 (d)(2)(3), dated January 1, 1995.



We concluded that FNS needs to provide guidance to sponsors on the content of annual training and the methods of delivery that will be acceptable.

### **Ratio of Monitors to Providers**

Our current work has also shown that FNS needs to establish a required ratio of monitors to day care providers. There is no requirement that the sponsor employ a number of monitors commensurate with the number of homes it sponsors. Consequently, a sponsor has a financial incentive to hire as few monitors as possible. With this high ratio of homes to monitors, the resulting reviews of providers are inadequate. Our unannounced visits to over 3,200 providers and centers nationwide has shown that, generally, providers and centers are not complying with program requirements (see exhibit D).

For example, the sponsor Angela's Angels Preschool, Inc. (Audit Report 27010-2-SF) did not adequately monitor operations in its homes. This occurred because the sponsor did not have enough staff to perform all required provider reviews in a sufficiently thorough manner.

As part of Angela's agreement with the State agency, sponsors accept final administrative and financial responsibility for program operations in their homes. To meet this responsibility, sponsors are required to conduct onsite monitoring reviews. These reviews assess compliance with meal patterns (mandatory meal components), recordkeeping, and other program requirements.<sup>7</sup>

Each home must be visited at least three times a year, with not more than 6 months between visits. Effective monitoring is an essential aspect of program oversight. It helps ensure that claims are correct by making sure providers keep the records they need to prepare accurate claims.

According to Angela's Angels' records, the sponsor completed 522 reviews of 200 providers during fiscal year 1995. According to the sponsor's records, 96 percent of these reviews were performed by

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<sup>7</sup>CFR 226.16 (d)(4)(i), dated January 1, 1995.

one monitor, a part-time employee working only about 600 hours during the year.

We concluded that the reviews that were performed were not sufficiently thorough to identify deficiencies in providers' operations: the sponsor did not document a single deficiency in any of its reviews. We found this same condition at most of the sponsors we reviewed; the sponsors' monitors seldom found the problems that our reviewers found.

We also found that the problem employees at the sponsors are usually not the monitors and administrative personnel, but the higher level employees--directors, assistant directors, etc. These employees have been able to divert funds for their own personal use because there is no requirement that they spend it on anyone else, such as their monitors.

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## **RECOMMENDATION NO. 4a**

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Issue regulations that: (1) define the level of outside employment that will not affect the adequacy of sponsor staffing, and (2) define the content of annual provider training and the acceptable methods of delivery.

### **FNS Response**

In its written response to the draft report, dated July 27, 1999, FNS stated

4a(1) FNS does not believe that this issue can be framed in terms of regulatory requirements, except that which already exists regarding the necessity of adequate staffing to perform required Program responsibilities. Will be addressed in guidance in the Fall 1999.

4a(2) A proposed integrity rule to be published in the Fall 1999.

### **OIG Position**

4a(1) In order to reach management decision, please provide a specific plan of action to be taken on this recommendation and the proposed completion date.

4a(2) In order to reach management decision, please provide specific details from the published proposed rule which address this recommendation and the proposed issuance date for the final rule.

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## **RECOMMENDATION NO. 4b**

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Develop and distribute a sponsors' handbook for administrative management of the CACFP that incorporates all Federal regulations controlling sponsorship of the program and that identifies the costs that are allowable for travel, car leasing, and employee benefit packages.

### **FNS Response**

In its written response to the draft report, dated July 27, 1999, FNS stated, "FNS will consolidate and update existing Program guidance in the Winter 2000."

### **OIG Position**

We accept management decision on this recommendation.

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## **RECOMMENDATION NO. 4c**

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Establish a required ratio of monitors to homes or increase the number of annual visits which must be made to homes and centers.

### **FNS Response**

In its written response to the draft report, dated July 27, 1999, FNS stated, "A proposed integrity rule to be published in the Fall 1999."

### **OIG Position**

As shown in this audit report lack of effective monitoring of providers and centers is pervasive in the CACFP. FNS needs to decrease the number of homes and centers monitors are required to visit; by requiring sponsors to hire more monitors or by increasing the required visits to the homes and centers which would ultimately have the same effect.

In order to reach management decision, please provide specific details from the published proposed rule which address this recommendation and the proposed issuance date for the final rule.

### **III. CACFP PROVIDERS DO NOT REPORT ALL CHILD CARE INCOME WHEN APPLYING FOR FOOD STAMPS AND CACFP ASSISTANCE**

#### **FINDING NO. 5**

Many child care providers claiming reimbursement for meals served to their own children, based on their participation in the Food Stamp Program (FSP) or other welfare programs, underreported their child care income to the State FSP agency. By not fully reporting their income, these providers may have received more FSP benefits than they were entitled to, or they may have been ineligible for any FSP benefits. In the latter case, the providers would also be ineligible to claim meals served to their own children under the CACFP. (We reported this issue to FNS management in a June 4, 1997, management alert.)

According to 7 CFR 226.15, providers may claim reimbursement for meals served to their own children if: (1) the household is receiving welfare benefits, such as FSP benefits, (2) household income does not exceed specified levels, or (3) the enrolled child is a foster child. To be determined eligible, a provider completes an "income eligibility statement," which must be reviewed and approved by the CACFP sponsor under which the provider participates. If claiming eligibility based on FSP participation, the provider reports his or her FSP case number on the statement. If claiming eligibility based on household income, the provider reports the names of household members and the amounts and sources of their income. In neither case is the sponsor required to verify the information reported.

For food stamp purposes, providers are considered self-employed, and the income they receive from parents for providing day care for their children, less their child care expenses, should be reported as self-employment income. Eligibility for FSP benefits and the amount of the benefits depend in part on the amount of income reported by the participant.

Our audit disclosed that the controls over CACFP providers who receive benefits simultaneously from both the CACFP and the FSP are inadequate. State FSP agencies are unaware of providers' day

care income unless the providers have reported this income themselves. State FSP agencies may be unaware of the providers participation in the CACFP, and the possibility that they are receiving child care income, because this information is not reported to them by either sponsors or the State CACFP agency.

As part of our CACFP audit, we selected a sample of 24 providers, participating under 3 sponsors in 2 States, who had applied to claim meals served to their own children based on their participation in the FSP. We contacted the State FSP agency to verify their participation in the FSP. While we found that generally these providers were participating in the FSP, we also found that at least 14 of them either underreported their day care income to the State FSP agency or did not report it at all. If these providers were to report all of their income, either they would not qualify for the amount of benefits they were receiving, or they would be ineligible to participate in the FSP. If they were ineligible for the FSP, they would not be eligible to claim meals served to their own children.

We provided the State FSP agencies details of these 14 cases of potential FSP fraud. Officials from both States indicated that they will pursue potential FSP fraud in these cases.

We also question whether individuals who do not report their financial situations accurately in order to gain eligibility should be allowed to participate in another FNS program.

As far as we could determine, there were no records available, except at each individual sponsor, to determine the potential extent of this problem. Based on our review, we believe that the problem may be widespread. Its impact will be exacerbated under the provisions of the Personal Responsibility and Work Opportunity Reconciliation Act of 1996, as amended. Under this act, providers will be categorized as either "tier 1" or "tier 2" providers. Tier 1 providers will be eligible to claim maximum meal reimbursement for all children, including their own, under their care. However, for tier 2 providers the rate of reimbursement will be individually determined for each child and may be lower than for tier 1.

Under tiering, all children in a home of a provider who is participating in the FSP would be eligible for tier 1 including the provider's children. Because tiering can affect all children under a provider's care, it will have a significant impact on future program costs. While

under the new rules, sponsors must verify income of tier 1 providers who claim eligibility based on household income, there is no verification requirement if the provider claims eligibility based on FSP participation.

In the management alert, we recommended that:

1. FNS require all sponsors to provide to their State CACFP agencies, and to FNS for monitoring purposes, a listing of all of their providers claiming CACFP eligibility for their children based on FSP participation. This information should be readily available from the sponsors. State agencies should then be required to provide this information to their State FSP agency.
2. The State FSP agency should be required to verify all day care income that is or is not reported for food stamp eligibility. This could be part of the normal FSP verification process.

In its response to Recommendation No. 1, FNS stated that it would prefer to make a listing of all CACFP providers available to food stamp offices for their use in verifying a participant's income. Currently, each sponsor submits to its State agency a management plan which includes a list of all the sponsor's providers currently participating in the CACFP. FNS stated it would encourage all CACFP State agencies to share these lists with food stamp State agencies and local certification offices. However, FNS stated it would not be able to require these lists to be shared without proposing a regulatory change to 7 CFR Part 226.

In response to Recommendation No. 2, FNS stated that the food stamp State agency will be provided with a listing of all child care providers currently participating in the CACFP. FNS will issue guidance explaining that the listing is to be used as a means of ensuring that all income is reported to the food stamp office by these child care providers. FNS emphasized that verification of all gross nonexempt income was currently required.

As stated, this finding is significant because providers were found to be receiving excessive benefits in both the FSP and the CACFP because they were not accurately reporting their child care income. If regulatory changes are needed for FNS to require the sharing of

income information between two of its own programs, then FNS should propose a change to the program regulations.

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## **RECOMMENDATION NO. 5a**

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Propose regulatory changes to require all sponsors to provide to their State CACFP agencies, and to FNS for monitoring purposes, a listing of all their providers claiming CACFP eligibility for their children based on FSP participation. This information should be readily available from the sponsors. State agencies should then be required to provide this information to their State FSP agency.

### **FNS Response**

In its written response to the draft report, dated July 27, 1999, FNS stated

This recommendation will require additional discussion with OIG and with Food Stamp Program administrators, and my require legislative action as well.

### **OIG Position**

In order to reach management decision, please provide a specific plan of action to be taken on this recommendation and the proposed completion date.

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## **RECOMMENDATION NO. 5b**

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Require the State FSP agency to verify all day care income that is or is not reported for food stamp eligibility. This could be part of the normal FSP verification process.



### **FNS Response**

In its written response to the draft report, dated July 27, 1999, FNS stated

This recommendation will require additional discussion with OIG and with Food Stamp Program administrators, and may require legislative action as well.

### **OIG Position**

In order to reach management decision, please provide a specific plan of action to be taken on this recommendation and the proposed completion date.

#### **IV. SOME METHODS OF RECOVERING OVERPAYMENTS COULD RESULT IN UNFAIR REDUCTIONS IN REIMBURSEMENTS**

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##### **FINDING NO. 6**

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At least one State agency had a practice of recovering overpayments and administrative claims from sponsors using a process which may have adversely affected the sponsors' providers and day care centers and the children they served. (We reported this in a July 24, 1998, management alert to the FNS Administrator and notified him that the practice may have national implications.)

In California, the California Department of Education (CDE) collects overpayments due from sponsors by offsetting the amounts owed against the sponsors' claims for reimbursement. The amounts owed are usually the results of ineligible administrative or meal claims identified through an audit or review, or because of outstanding program advances. While this practice may seem logical, the amounts being offset are the food reimbursements due to centers and providers who in all likelihood were not responsible for the overpayments or advances. Offsets like this may directly harm the children in the program.

For example, if CDE auditors found that a sponsor did not have records supporting administrative or food payments that were made for a previous claim period, they calculated an overpayment and reduced the sponsor's next claim. If the sponsor did not receive the next claim, or only received a portion of it, the sponsor did not have funds to pay the food claims of its centers and providers. There was usually no direct correlation between who caused the overpayment and who made the repayment.

A situation like this was reported to the FNS Western Regional Administrator in a management alert dated October 29, 1997. In that case, CDE was collecting advances to a sponsor, the Community Business Improvement Association, Inc., of Pasadena, California, by offsetting current claims for reimbursement.

We believe this practice may be taking place in other States. Program regulations do not appear to directly address the issue of how overpayments and advances should be collected. Title 7 CFR 226.7 empowers the State agencies to establish procedures to recover outstanding advances. Title 7 CFR 226.8 states that a State agency shall deduct overpayments from unpaid claims for reimbursement, but the regulation does not specifically say how this should be done.

Another example was disclosed during our audit of the defunct sponsor, Aladdin Child Care Services, Inc., (Aladdin) of Inglewood, California. This sponsor was selected for audit because it had withdrawn from the CACFP, effective September 30, 1997, while still owing many of its day care centers substantial amounts of program funds. When the sponsor withdrew, it still owed an August payment of \$34,383 to its providers and centers.

We found that CDE retained the August 1997 payment to recover part of a \$208,160 overpayment that had been identified during a CDE audit of the years 1994, 1995, and 1996. We also found that during the period March 1996 through December 1997, CDE had offset another \$83,889 from Aladdin to recover a separate overpayment identified during an earlier program review. The total amount of offsets against this sponsor was \$118,271.49.

Our primary concern with this practice is that CDE takes the food funds which are owed to all providers and child care centers to settle the debts owed by the sponsor, without determining who actually owes the debts. As a result, providers are not reimbursed for costs incurred for participating in the CACFP and eligible children could be adversely affected.

As is evident from the Aladdin case, CDE recovered overpayments identified as far back as 1994 from payments due to providers and centers in 1997. We found no effort on the part of CDE to trace the overpayments to who actually caused the problem--specific providers and centers, or the sponsor itself.

We understand CDE's desire to recover funds owed by Aladdin. However, we question the method used by CDE to recover these funds. We believe that if the overpayment occurred because the sponsor claimed ineligible administrative costs, then the recovery should come directly from the sponsor's administrative funds.

Similarly, if any particular provider or center was at fault, then the recovery should come from that particular provider or center. The current method of a blanket offset of future reimbursements harms legitimate providers and centers and the children under their care.

In our management alert, we made the following recommendations to the FNS National Office:

1. Issue guidance to CDE so that the recovery of ineligible program funds from sponsors comes from the entities which are directly responsible for the ineligible amounts being claimed. Ineligible provider payments should come from the providers at fault. Ineligible sponsor payments should come from the sponsor.
2. Ask other States how they collect CACFP claims against sponsors/providers, and issue the same guidance to these States, if necessary.

In response to this management alert, the FNS Acting Administrator stated that FNS would issue guidance to Regional offices and State agencies on appropriate recovery procedures for debts arising from unallowable operating and/or administrative charges to the CACFP.

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## **RECOMMENDATION NO. 6**

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Issue guidance so that the recovery of ineligible program funds from sponsors comes from the entities which are directly responsible for the ineligible amounts being claimed. Ineligible provider payments should come from the providers at fault. Ineligible sponsor payments should come from the sponsor.

### **FNS Response**

In its written response to the draft report, dated July 27, 1999, FNS stated

FNS will continue through the Winter 1999 to explore ways of dealing with this concern with OIG, OGC, and State agency administrators.

### **OIG Position**

In order to reach management decision, please provide a specific plan of action to be taken on this recommendation and the proposed completion date.

## V. FNS SHOULD RAISE THE VISIBILITY OF THE CACFP

### FINDING NO. 7

Parents of children in day care could be used as an effective control to report on the status of the CACFP. FNS should raise the visibility of the program so that parents, who may be physically at the provider homes and centers on a daily basis, are aware of the nutritional standards that meals provided there should meet. In our opinion, FNS cannot rely solely on sponsor oversight given the extent of problems we have found with it.

We have found that parents of children in day care may be unaware that the meals served to their children are being subsidized under the CACFP and as such, that these meals must meet certain nutritional standards. In fact, OIG employees who were working on the various CACFP audits and who had children in day care were often unaware that their own children were being served CACFP-meals.

While we have seen some indication that sponsors may be notifying parents, either through the application process or through the tiering determination, that their children are participating in the CACFP, some type of notification at the providers' home or child care center would be a good reminder. This reminder would notify parents that CACFP-qualified meals are being served. We believe that FNS should create signs or posters for each of the approximately 227,000 providers and centers that would encourage parental input. The posters might say, for example:

Meals served to your children at this day care facility are being subsidized by the United States Department of Agriculture under the Child and Adult Care Food Program and, as such, must meet certain nutritional requirements. If you have any concerns about the meals served to your children or questions about this program, please call (State agency or FNS).

Providers and Child Care Centers are required to post their licenses to operate their day care facilities and these licenses stipulate any licensing restrictions. It is not unreasonable to provide these same facilities with a CACFP sign or poster and require that it be

prominently displayed. A well designed poster would also help FNS meet one of its primary goals of promoting good nutrition.

Exhibit D shows the results of over 3,200 unannounced visits we made to day care providers and centers nationwide. As shown, much more needs to be done to improve the monitoring and training of providers and centers serving children and adults eating USDA-funded meals while in day care. One way to improve monitoring is to use the oversight of the parents. If the parents are aware that their children are to be served nutritious meals according to USDA guidelines and have a method available to report any concerns they might have, we believe that such additional oversight could prove effective in assuring program requirements are met.

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## **RECOMMENDATION NO. 7**

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Instruct the State agencies to provide some mechanism to inform parents of the participation of their day care providers in the CACFP and encourage their awareness of the activities of those providers.

### **FNS Response**

In its written response to the draft report, dated July 27, 1999, FNS stated, "FNS will address in Program guidance in the Fall 1999."

### **OIG Position**

In order to reach management decision, please provide a specific plan of action to be taken on this recommendation and the proposed completion date.

## **EXHIBIT A - ANNUAL FUNDING FOR TERMINATED SPONSORS**

State	Sponsor No.	Annual Funding
<b>California</b>	1	\$ 721,344
	2	1,536,601
	3	3,115,319
	4	4,582,364
	5	7,596,143
		\$17,551,771
<b>Florida</b>	6	850,336
<b>Idaho</b>	7	54,215
<b>Louisiana</b>	8	736,278
<b>Michigan</b>	9	5,619,904
<b>Ohio</b>	10	1,902,680
<b>Pennsylvania</b>	11	1,207,759
	12	2,530,081
		3,737,840
<b>Utah</b>	13	1,740,803
<b>Oregon</b>	14	1,921,441
<b>Tennessee</b>	15	267,261
	16	169,047
		436,308
<b>Total</b>		\$34,551,576 <sup>1</sup>

<sup>1</sup>Funds To Be Put To Better Use.



**EXHIBIT B - SUMMARY OF THE STATUS OF INVESTIGATIONS IN PROCESS AS OF FEBRUARY 19, 1999**

State	Investigations in Process	Individuals Indicted or Named in Criminal Informations	Individuals Who Pled Guilty or Were Convicted	Individuals Sentenced
Arizona	1	1	1	1
California	8	19	13	13
Colorado	1			
Florida	2			
Idaho	1	1	1	1
Louisiana	2			
Michigan	1	2		
New Mexico	2	1	1	1
New York	2	1	1	1
Ohio	2	11	7	7
Pennsylvania	3	1	1	
Tennessee	3	3	1	1
Utah	1	4	1	
Washington	2		1	1
<b>TOTALS</b>	<b>31</b>	<b>44</b>	<b>28</b>	<b>26</b>

## **EXHIBIT C - SUMMARY OF AUDITS AND INVESTIGATIONS**

<b>Summary of Audits and Investigations</b>								
<b>Sponsor Reviews</b>		<b>Sponsor met Seriously Deficient criteria</b>	<b>Types of Program Deficiencies Identified</b>				<b>Results</b>	
<b>State</b>	<b>No.</b>		<b>Monitoring/ Training</b>	<b>Administrative Costs</b>	<b>Provider Payments</b>	<b>Bogus Providers /Children</b>	<b>Sponsor Terminated</b>	<b>Investigated for Fraud</b>
AL	1	1	1					
AR <sup>1</sup>	2		1					
AZ	3	2	2	2		1		1
CA	11	11	10	11	4	3	5	8
CO	2	2		1		1		1
FL	2	2	1	2			1	2
ID	1	1		1			1	1
IL	4	3	3					
IN	2							
LA	3	2	2	2		2	1	2
ME	1	1	1	1				
MI	1	1		1			1	1
MO	1		1					
NC	1		1					
NM <sup>2</sup>	3	1	1	1	1			2
NY	2	1	1	1				2
OH <sup>3</sup>	2	1	1			1	1	2
OR	1	1	1	1			1	
PA <sup>4</sup>	3	2	1	2	1		2	3
TN	3	2		2		1	2	3
UT	2	1	2	2		1	1	1
WA <sup>5</sup>	2	1	1	1				2
WI	2	1	1					
<b>TOTAL<sup>6</sup></b>	<b>55</b>	<b>37</b>	<b>32</b>	<b>31</b>	<b>6</b>	<b>10</b>	<b>16</b>	<b>31</b>

1. Includes sponsor employee.
2. Includes sponsor employee and day care home provider.
3. Includes one day care home provider.
4. Includes one day care home provider.
5. Includes one day care home provider.
6. Total includes 49 sponsors (includes 1 day care center), 2 employees, and 4 providers.

## EXHIBIT D - RESULTS OF PROVIDER VISITS

Sponsor	Attempted Provider/ Center Visits	Review Completed	Number Concerns Noted	Type of Concern Noted			
				Record Keeping	Possible Overclaim	Health/ Safety Issues	Meal Components
Quad County Child Nutrition Program	115	107	65	X	X	X	
Feeding Arizona Kids, Inc.	61	51	46	X	X	X	X
BJ Enterprises, Inc.	76	57	47	X	X	X	X
Angela's Angels Preschool, Inc.	158	125	75	X	X	X	
Pacific Asian American Family Care, Inc.	108	86	49	X	X	X	
Ken-Kia Child Development, Inc.	99	86	82	X	X	X	
Lunch, Inc.	77	75	12	X	X		
Southern Maine Christian Day Care Services	114	114	101	X	X	X	
Connections, Inc.	105	75	63	X	X	X	
New Jerusalem Church of God in Christ	123	67	53	X	X	X	X
Child Care Services, Inc.	84	72	51	X	X	X	X
Children of the Future	205	144	134	X	X	X	X
Children's Spectrum Child Care Services, Inc.	270	187	122	X	X	X	X
A Perfect Balance, Inc.	43	40	24	X	X	X	X
Human Development Center	88	88	53	X	X	X	
YWCA of Metropolitan Chicago	56	56	52	X	X		
Sage Community Providers, Inc.	125	93	77	X	X		
Child Nutrition Services, Inc.	379	379	116	X	X		
Cape Fear Tutoring, Inc.	176	173	50	X	X		
Children's Best Interests, Inc.	232	209	112	X	X	X	X
Operation Kids, Inc.	46	46	0				
Community Business Improvement Association,	119	57	44	X	X		X
King County Family Child Care Association	28	22	4	X		X	
Community Relations - Social Development	27	27	21	X	X		
Family Day Care Services, Inc.	171	166	117	X	X	X	X
Aladdin Child Care Services <sup>2</sup>	N/A	N/A	N/A	N/A	N/A	N/A	N/A
New Life For Children	203	203	93	X	X		X
<b>TOTAL</b>	<b>3,288</b>	<b>2,805<sup>1</sup></b>	<b>1,663</b>				

<sup>1</sup>Four hundred and eighty-three visits were not completed largely because there was nothing to review: the home was no longer in the program, or no one was on the premises during the stated food service hours.

<sup>2</sup>Visits were not conducted at Aladdin because the sponsor had terminated operation prior to our joint audit and investigation.

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# EXHIBIT E - FOOD AND NUTRITION SERVICE'S WRITTEN RESPONSE TO THE DRAFT REPORT



JUL 27 1999

United States  
Department of  
Agriculture

Food and  
Nutrition  
Service

3101 Park  
Center Drive  
Alexandria, VA  
22302-1500

**SUBJECT:** Official Draft Audit Report Number 27601-7-SF,  
Presidential Initiative: Operation Kiddie Care

**TO:** James R. Ebbitt  
Assistant Inspector General for Audit  
Office of Inspector General

We appreciate the opportunity to comment on the official draft of the subject Child and Adult Care Food Program (CACFP) audit report and request that this correspondence, as well as its attachments, be included in the final report. The Food and Nutrition Service (FNS) is committed to improving the operations of the CACFP, and will continue to aggressively pursue all means to ensure sound program management as well as correct any problems of mismanagement and fraud. Further, FNS continues to recognize that access to quality and affordable child care is a major pillar of welfare reform and is clearly an important aspect of this Administration's emphasis on quality child care. Since CACFP requires licensing, training, nutrition standards and actual home visits, participation in this nutrition program is widely viewed as a significant indicator that quality child care is being provided.

This audit was initiated because CACFP State agencies and FNS requested the Office of Inspector General (OIG) to review certain sponsors which appeared to have seriously deficient operations. OIG has done a very thorough job of investigating and auditing the sponsors. In the course of these audits, OIG has recommended review of the basic program structure of CACFP with the goal of eliminating fraud and/or mismanagement. We agree with this goal. Our challenge is to:

- develop fraud deterrent policies and procedures which State and Federal agencies can successfully monitor;
- provide the training and guidance that State agencies and sponsors need up front so that they know what the program rules and regulations are;
- terminate any sponsor who refuses to comply with program rules; and
- develop a basic structure for CACFP that provides nutritious foods for children and safe and quality care that parents can rely on; ensures that government funds are well spent; and enables State agencies and sponsors to effectively run quality programs.

A synopsis of the actions, both taken and in progress, by FNS related to management improvement in CACFP is attached (Attachment 1).

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Exhibit E - Page 1 of 15

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## **EXHIBIT E - FOOD AND NUTRITION SERVICE'S WRITTEN RESPONSE TO THE DRAFT REPORT**

James R. Ebbitt

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We recognize and appreciate the valuable contribution made by OIG in assisting FNS and State agencies in identifying seriously deficient sponsors. Despite our large-scale commitment of resources to implementing the statutorily mandated tiered reimbursement system and the afterschool snack program, and despite the steady decrease in the Agency's available resources since the late 1970s, FNS has worked conscientiously to make management improvements in CACFP. As a first step toward improving the overall management of CACFP, FNS issued comprehensive packages entitled Management Improvement Guidance (Guidance) for sponsors of family day care homes and centers in 1997 and 1998, respectively. The Guidance packages were developed by a Federal-State task force to assist States and sponsoring organizations with such vital functions as developing, analyzing and approving sponsoring organizations' budgets and management plans. We also have developed a management assessment guide (Attachment 2) which describes some of the more common indicators of mismanagement that have been identified in reviews and audits. This guidance provides State reviewers with a visual tool that helps to identify problems that should be evaluated to determine if a violation has occurred and what corrective actions would be appropriate. State agencies should find this management assessment guide a useful tool in ferreting out unscrupulous sponsors. State agencies do receive special audit funds to verify whether sponsors are complying with the rules. Unfortunately, OIG staff have found some instances of fraud even after a State agency audit. This should help focus State agencies on specific indicators of potential fraud or mismanagement. This OIG audit in effect demands that State agencies and FNS devote significantly greater resources to the investigative role than the audit review role. Finally, as detailed in our June 7, 1999, letter to Inspector General Viadero, we will soon issue a regulatory proposal which addresses many of the program changes recommended in your audits. Thank you for your letter of July 12, 1999, in which you provided comments on the draft proposed rule. We are considering several of your comments for incorporation in the proposal.

In an attempt to secure the resources necessary to properly address the management problems identified in CACFP, the Department last year requested that 1/8 of 1 percent of program expenditures be reserved for management improvement activities. Congress approved a portion of the funding requested; \$1 million a year for 5 years rather than the approximately \$2 million requested. We are utilizing these funds for an extensive effort currently under way for training program operators at all levels. To ensure that the Guidance is implemented consistently throughout the program, we will be conducting five training sessions. The first of these is designated for Federal staff and will occur in September 1999. Four additional sessions for State agency staff will be held from October 1999 through January 2000. In the fall of 1999, we will begin Phase 2 of this training effort which will be the development of training modules for State agency use in training local program operators. The funding provided by Congress is also being used by each of the seven FNS regional offices to support regional plans specifically targeted to program management improvement.

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## **EXHIBIT E - FOOD AND NUTRITION SERVICE'S WRITTEN RESPONSE TO THE DRAFT REPORT**

James R. Ebbitt  
Page 3

State agencies play a critical role in ensuring proper management of CACFP and protecting the program against fraudulent operators. Indeed many of the problem-prone sponsors reviewed in the OIG audit were originally identified by FNS and State agencies. We do, however, acknowledge that, although a great deal of program guidance has been issued, some State program administrators have been reluctant or unable to actually implement the changes recommended in the guidance.

State agencies are the partners of FNS in CACFP administration. If a policy of "zero tolerance for fraud" is going to be successfully implemented, it can only happen if FNS and State agencies are working effectively as a team. OIG can and should play a positive role by providing information and resources to this effort. FNS will provide the leadership and technical assistance that States need to successfully administer CACFP but, in the final analysis, States must do the application reviews, training, monitoring, corrective action, and termination. Based on legislative and regulatory requirements, the guidance builds a strong platform for effective program management and oversight. We believe that, as a result of the availability of new management improvement resources and the priority being placed on management improvement by Agency leadership, we will be better able to ensure that existing and forthcoming guidance and regulations are properly and promptly implemented throughout the country.

While we agree with and accept most of the draft audit report's findings and are committed to continuing our efforts to improve management in the CACFP, we do not accept the draft audit's implication that this Agency has not responded to program management or integrity problems, either before or after the commencement of Operation Kiddie Care. FNS has for over 15 years maintained a list of those CACFP institutions that have been terminated from the program as a result of serious deficiencies. This listing is regularly updated and is one important tool which State agencies use to determine the eligibility of organizations applying to participate in CACFP. Even before the beginning of Operation Kiddie Care, there were over 200 organizations on the list. Since Operation Kiddie Care began, States have requested that FNS add another 200 organizations to the list. Very few of these were placed on the list as a result of Operation Kiddie Care audits or investigations. The efforts which we already have under way will ensure that program cooperators at all levels make the needed program improvements. We at FNS will continue to work closely with OIG in their ongoing audit and investigative work, and will continue to urge State cooperators to do the same. We are also committed to evaluating all aspects of program structure and operations. To this end, we will convene a group of State Administrators, community-level cooperators, and representatives from the Library of Congress, the Department of Health and Human Services, and Congressional staff to examine program structure and make recommendations for changes.

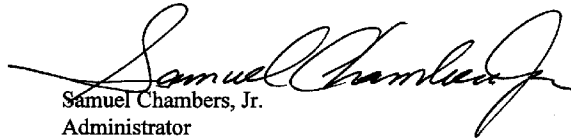
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**EXHIBIT E - FOOD AND NUTRITION SERVICE'S  
WRITTEN RESPONSE TO THE DRAFT  
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James R. Ebbitt  
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Attached, please find responses to each of the audit recommendations which describe our planned action and timeframes for completion (Attachment 3). Based on this information, we are requesting management decision on all of the audit recommendations.

Please contact us if you need additional information.

  
Samuel Chambers, Jr.  
Administrator

Attachments

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# EXHIBIT E - FOOD AND NUTRITION SERVICE'S WRITTEN RESPONSE TO THE DRAFT REPORT

Attachment 1  
July 1999

## Child and Adult Care Food Program (CACFP) Food and Nutrition Service Actions Related to Management Improvement

### ACTIONS COMPLETED

#### Policy/Guidance

- Issued comprehensive CACFP Management Improvement Guidance for family day care home sponsoring organizations and child care centers. This guidance was developed by the Federal-State Task Force over a period of more than 2 years to address the operational problems identified through reviews and audits. (family day care home guidance issued May 1997; center guidance issued February 1998)
- Assisted OMB and the Department from January 1997 through March 1999 in the development of an improved single audit compliance supplement for audits of CACFP institutions. (initial revision published May 1998; updated revision published April 1999)
- Assisted OIG in revising and reissuing the CACFP Audit Guide, which non-Federal auditors use to conduct program-specific audits of institutions operating the CACFP. (issued March 1999)
- Regularly update and issue the "seriously deficient" list for use by State agencies during the institution approval process. The list includes CACFP institutions that have been terminated from the Program. (ongoing)
- Targeted monitoring efforts in CACFP as a critical area of review in the Management Evaluation guidance that is issued annually to Regional offices to better focus FNS reviews of State agencies to areas identified as potential problems. (1995, 1996, 1997, 1998 and 1999)
- Developed and distributed to State agencies a management assessment guide which outlines and describes some of the more common characteristics or indicators of abuse or mismanagement that have been identified in reviews and audits. (May 1999)
- Issued guidance to State agencies instructing them to inform centers that they may participate as independent centers (as opposed to being sponsored) under a direct agreement with the State agency. Correspondence was sent by each of the regional offices to their respective State agencies. (April - September 1998)
- Issued policy on the expanded use of 1.5% audit funds. (February 22, 1999)

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# **EXHIBIT E - FOOD AND NUTRITION SERVICE'S WRITTEN RESPONSE TO THE DRAFT REPORT**

- Issued guidance on the use of unannounced visits in the CACFP. (July 2, 1999)
- Issued guidance on pre-approval visits by State agencies to new private institutions applying to participate in CACFP. (July 14, 1999)

### **Proposed Changes to CACFP Regulations**

Drafted and entered into formal clearance a proposed rule designed to improve CACFP operations and monitoring at the State and institution levels and, where possible, to streamline and simplify Program requirements for State agencies and institutions. The changes in the proposed rule address the problems uncovered by State and Federal Program reviews and OIG audits and investigations. (Proposed rule is currently in Departmental clearance; publication expected by Fall 1999.)

### **Legislation**

- Requested and secured an appropriation from Congress for Fiscal Years 1999-2003 in the amount of \$1 million per year for CACFP management improvement efforts. A significant portion of the funds has been provided to regional offices to improve Program management through additional monitoring, training, and technical assistance. Each regional office has implemented an action plan for the use of the funds. Additional staff have been hired to increase the Federal presence at both the State and local levels.
- Congress approved the following Departmental proposals related to CACFP management improvement:
  - ◆ Establishing a time limit on the participation by institutions that are moving towards tax-exempt status.
  - ◆ Providing State agencies with additional time to process institution applications. This change helps ensure that State agencies approve only well-qualified applicants.

### **Correspondence**

Sent a letter from the Deputy Administrator to each CACFP State agency Director. The letter expressed concern regarding management weaknesses and abuse in the CACFP, and provided the management assessment guide which outlines common characteristics or indicators of Program abuse or mismanagement. (May 7, 1999)

Sent a letter from the Under Secretary to each CACFP State agency Commissioner/Superintendent. The letter expresses the Department's concerns about the OIG audit findings as well as emphasizes the need to strengthen Program management. (June 2, 1999)

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# **EXHIBIT E - FOOD AND NUTRITION SERVICE'S WRITTEN RESPONSE TO THE DRAFT REPORT**

## **Speeches to CACFP Operators**

The following speeches were made to State and local-level operators about the importance of improving CACFP Program integrity:

Under Secretary Watkins speech to the CACFP Sponsor's Association Conference, Milwaukee. (September 1997)

Deputy Under Secretary Paradis speech to the National Association of CACFP Professionals (State agencies) Conference, New Orleans. (March 1998)

Under Secretary Watkins speech to the CACFP Sponsor's Association Conference, Dallas. (September 1998)

Deputy Under Secretary Paradis speech to the Western Region Sponsor's Roundtable conference, Universal City, California. (October 1998)

Under Secretary Watkins speech to the CACFP Sponsor's Forum Conference, Atlanta. (May 1999)

## **CACFP Management Improvement Task Force**

In July 1994, FNS presented the Under Secretary with plans for a Federal/State agency Task Force for the purpose of making recommendations for Program management improvements. The Task Force was part of the CACFP Initiative begun by FNS to: improve Program integrity; streamline the operations at the State and local levels; and maintain a Program which is fully open to all well-managed sponsoring organizations and the children they serve.

Federal representatives met to discuss goals of Task Force. (January 1995)

Meetings of entire Task Force. (March 1995; September 1995; September 1996)

Task Force teams worked on development of CACFP Management Improvement Guidance for day care home and centers. (March 1995 to February 1998)

Expanded Task Force (which included local Program operators and representatives of national CACFP organizations and advocacy groups) met. (February 1999)

Task Force Training Team Members met to develop national training for CACFP State agencies. (April 1999; June 1999)

## **Training**

Currently developing Phase 1 of a nationwide training program which focuses on State agency program oversight. To accomplish this, a team of State and Federal representatives are developing training modules to be used to train all Federal and State agency staff involved in the administration or operation of CACFP. Phase 1 of the training program will take place from

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## **EXHIBIT E - FOOD AND NUTRITION SERVICE'S WRITTEN RESPONSE TO THE DRAFT REPORT**

September 1999 to January 2000. Several hundred attendees are expected at these sessions which have been scheduled as follows:

- Training session for Federal staff (Kansas City, Missouri, September 22-24, 1999)
- Training session for Mountain Plains Regional Office State agencies (Omaha, Nebraska, October 20-22, 1999)
- Training session for Southeast and Southwest Regional Office State agencies (New Orleans, Louisiana, November 8-10, 1999)
- Training session for Midwest, Northeast and Mid-Atlantic Regional Office State agencies (Columbus, Ohio, November 16-18, 1999)
- Training session for Western Regional Office State agencies (Bay Area, CA, January 11-13, 2000)

Phase 2 of the training program is scheduled to begin in the fall 1999. Under Phase 2, training modules will be developed for State agency use in training local Program operators. Child care community representatives (operators and advocates) will be asked to join the team of Federal and State representatives to develop the modules for State use.

### **ACTIONS IN PROGRESS**

- Currently working on the development of Program materials which include requests made by the Task Force at the February 1999 meeting. Items currently under development include:
  - ◆ Revision of the FNS handbook for family day care homes
  - ◆ Revision of the CACFP financial management instruction, FNS 796-2
  - ◆ Update of previous policy on CACFP seriously deficient providers to reiterate procedures that should be followed
  - ◆ Procedures relating to immediate termination of institutions
  - ◆ Guidance for approving CACFP center sponsor administrative budgets
  - ◆ Guidance on CACFP funds integrity
  - ◆ Guidance on training in CACFP
  - ◆ Facility poster designed to increase Program awareness

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## **EXHIBIT E - FOOD AND NUTRITION SERVICE'S WRITTEN RESPONSE TO THE DRAFT REPORT**

- ◆ Letter to new CACFP facilities which includes procedure for reporting Program violations
- ◆ Key elements for use by State agencies in the institution approval process
- ◆ Key elements of reviews of institutions
- ◆ Brochure on obtaining professional and consultant services
- ◆ Board of directors fact sheet
- ◆ Best Practices Awards to recognize and promote well-managed State agencies and sponsors
- ◆ Participation at Upcoming National Conferences
  - ◆ CACFP Sponsor's Association annual conference in Boston, Massachusetts in September 1999
  - ◆ Western Region Sponsor's Roundtable conference in Oakland, California in October 1999
  - ◆ National School Lunch Program State Directors bi-annual conference in San Antonio, Texas in December 1999

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# EXHIBIT E - FOOD AND NUTRITION SERVICE'S WRITTEN RESPONSE TO THE DRAFT REPORT

Attachment 2

<b>Child and Adult Care Food Program (CACFP) Institutions</b> <b>Indicators of Potential or Existing Problems</b>			
Indicators	FDCH Sponsors	Center Sponsors	Independent Centers
<b>Board Oversight</b>			
Board of Directors consists entirely of family members	■	■	
Majority of members on the Board of Directors are sponsor officials	■	■	
Board of Directors is chaired by sponsor official	■	■	
Board minutes do not reflect policy and management oversight (e.g., establishing policy, approving expenditures, approving officer salary increases, audit review)	■	■	
<b>Budget/Claim for Reimbursement</b>			
Consistently claiming at or near the approved budget amount for an administrative cost item	■	■	
Year-to-date claims do not reflect approved budget	■	■	■
Questionable or potentially fraudulent meal claiming practice (e.g., block claiming, meals claimed when facility closed)	■	■	■
Excessive reimbursement retained for administrative costs		■	
<b>Operational Oversight</b>			
Does not have a qualified accountant or an adequate accounting information system	■	■	■
Lack of internal controls (e.g., inadequate separation of duties, position held by family member limits internal control)	■	■	■
Does not have official policies and procedures for hiring and terminating or for employee activities and benefits	■	■	
Related party transactions (e.g., director or family member is the owner of rented property housing CACFP facility)	■	■	■
Absentee management	■	■	■
<b>Monitoring/Training</b>			
Does not conduct unannounced monitoring visits/reviews have no findings	■	■	
Inadequate number of monitors to conduct required visits	■	■	
Implausible number of monitoring visits made on the same day	■	■	
Sponsor does not have administrative staff or provider/center staff training programs	■	■	
Sponsor does not require providers/center staff to attend training	■	■	
<b>Audits</b>			
Required audits are not performed	■	■	■
Management/Board of Directors do not follow-up on corrective action needed	■	■	■
<b>Other</b>			
Multiple requests from providers to transfer to another sponsor	■		
Rapid growth without appropriate increase in administrative staff	■	■	
Sponsor's income depends solely on CACFP administrative reimbursements	■		
Health and safety concerns reported from any source (e.g., parent complaints)	■	■	■

Food and Nutrition Service  
Child Nutrition Division  
May 7, 1999

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# EXHIBIT E - FOOD AND NUTRITION SERVICE'S WRITTEN RESPONSE TO THE DRAFT REPORT

Attachment 3  
July 1999

## Responses to CACFP Operation Kiddie Care Audit No. 27601-7-SF

**Recommendation No. 1:** Study alternative methods of delivering a meal program to needy children and adults in day care, specifically one that addresses the problems noted at private, nonprofit organizations. While the above study is underway and the program continues in its current form, FNS also needs to strengthen controls by implementing the recommendations provided at the end of Finding No. 2.

**FNS Response to Recommendation No. 1:** In the Fall 1999, a task force will be assembled to study alternative methods of delivering a meal program.

**Recommendation No. 2a:** Revise regulations to include standards for approving and renewing sponsors. Sponsors should have business experience, adequate management plans and budgets, demonstrate financial capability and a standard of ethics, and undergo a criminal background check.

**FNS Response to Recommendation No. 2a:** A proposed integrity rule to be published in the Fall 1999.

**Recommendation No. 2b:** Revise regulations to include standards for terminating sponsors. Sponsors should face termination for engaging in inappropriate business practices, falsifying program information, and concealing a criminal background.

**FNS Response to Recommendation No. 2b:** A proposed integrity rule to be published in the Fall 1999.

**Recommendation No. 2c:** Provide guidance to State agencies on the composition of governing boards of sponsors, and clarify the required oversight and independence of these boards.

**FNS Response to Recommendation No. 2c:** Addressed in the Agency's Management Improvement Guidance and in a management assessment guide (attached) which was distributed to SAs in May 1999. Developing a Board of Directors Fact Sheet which is to be completed and distributed in September 1999.

**Recommendation No. 2d:** Advise State agencies (SAs) that they currently have the authority to set administrative salary guidelines for employees of CACFP sponsors that are consistent with local salary structures.

**FNS Response to Recommendation No. 2d:** FNS will issue memorandum to SAs in the Fall 1999.

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## **EXHIBIT E - FOOD AND NUTRITION SERVICE'S WRITTEN RESPONSE TO THE DRAFT REPORT**

**Recommendation No. 2e:** Allow SAs to devote up to 20 percent of the required review time within a review cycle to additional reviews of new and problem sponsors. (For example, within a review cycle, if a State uses 100 staff days to accomplish CACFP review, it may shift 20 of these days to problem or new sponsors by diminishing review days used for other sponsors.)

**FNS Response to Recommendation Nos. 2e:** A proposed integrity rule to be published in the Fall 1999.

**Recommendation 2f:** Expand the authorized action against "seriously deficient" sponsors: (1) to allow for the immediate termination of a sponsor charged by another government agency (Federal, State, or local) with having placed the health or safety of a child in jeopardy; (2) to include sponsors whose agreement lapses prior to termination; (3) to require automatic termination or suspension of a sponsor for fraud.

**FNS Response to Recommendation 2f:** A proposed integrity rule to be published in the Fall 1999.

**Recommendation No. 2g:** Establish required review coverage and standardized reporting for sponsor monitoring of providers to include: (1) assessing whether enrollment, meal count, and menu records are current and complete and (2) reconciling observed attendance with enrollment data and with the subsequent meal count that is claimed.

**FNS Response to Recommendation No. 2g:** A proposed integrity rule to be published in the Fall 1999. Addressed in the CACFP management standards for family day care home sponsoring organizations which were published and distributed to SAs in May 1997.

**Recommendation No. 2h:** Explore alternative systems of administrative cost reimbursement so that they are not directly based on day care home numbers and do not create a financial disincentive to compliance enforcement. Consider emphasizing monthly budgeting and strengthening sponsor eligibility requirements.

**FNS Response to Recommendation No. 2h:** In the Fall 1999, a task force will be assembled to study alternative methods of delivering a meal program.

**Recommendation No. 2i:** Strengthen the provider regulations to require that all participating providers must receive a specified minimum number of hours in program training each year and required SAs to verify that providers received the prescribed training.

**FNS Response to Recommendation Nos. 2i:** A proposed integrity rule to be published in the Fall 1999.

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## **EXHIBIT E - FOOD AND NUTRITION SERVICE'S WRITTEN RESPONSE TO THE DRAFT REPORT**

**Recommendation No. 2j:** Require that SA administrative reviews of sponsors and day care homes include steps to identify recordkeeping deficiencies and inflated meal claims, and to assess the adequacy of sponsor monitoring of the homes. Reviews should include unannounced day care home visits and parent contacts.

**FNS Response to Recommendation 2j:** A proposed integrity rule to be published in the Fall 1999. Also, addressed in the CACFP management standards for family day care home sponsoring organizations which were published and distributed to SAs in May 1997.

**Recommendation No. 2k:** Require owners and officers to be bonded so that program funds lost through their inappropriate actions will be restored to the program.

**FNS Response to Recommendation No. 2k:** Office of Management and Budget (OMB) Circular A-102, Attachment B, prohibits Federal agencies from promulgating bonding requirements except when required by law. This issue will be analyzed as part of the larger study of Program re-design in the Fall 1999.

**Recommendation No. 3a:** Determine from the Office of General Counsel (OGC) whether it is legal for sponsors to recover administrative costs by retaining a portion of the funds earned by centers providing food to children.

**FNS Response to Recommendation No. 3a:** FNS will seek legal opinion from the Office of General Counsel by the Summer 1999.

**Recommendation No. 3b:** Notify all child care centers that participate under sponsors that they have the option to participate directly with the SA.

**Recommendation No. 3c:** Inform centers that if they choose to participate under a sponsoring organization (SO), the SO may retain a portion of their food reimbursement to cover their administrative costs. Clarify the exact amount of administrative costs involved.

**FNS Response to Recommendation Nos. 3b and 3c:** Completed. FNS issued guidance on April 20, 1998 to SAs instructing them to inform centers that they may participate as independent centers (as opposed to being sponsored) under a direct agreement with the SA. They were also informed to let centers know that if they chose to participate under a sponsoring organization, a portion of their food reimbursement may be retained by the sponsoring organization to cover administrative costs. FNS will have training from September 1999 to January 2000.

**Recommendation No. 3d:** Establish a realistic rate that sponsors can retain for administering the program to the centers. The rate should more closely equal what a sponsor is paid to administer the program for day care providers.

**FNS Response to Recommendation No. 3d:** A proposed integrity rule, to be published in the Fall 1999, incorporates performance standards which address allowable cost.



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## **EXHIBIT E - FOOD AND NUTRITION SERVICE'S WRITTEN RESPONSE TO THE DRAFT REPORT**

**Recommendation No. 4a:** Issue regulations that: (1) define the level of outside employment that will not affect the adequacy of sponsor staffing, and (2) define the content of annual provider training and the acceptable methods of delivery.

**FNS Response to Recommendation No. 4a(1):** FNS does not believe that this issue can be framed in terms of a regulatory requirement, except that which already exists regarding the necessity of adequate staffing to perform required Program responsibilities. Will be addressed in guidance in the Fall 1999.

**FNS Response to Recommendation No. 4a(2):** A proposed integrity rule to be published in the Fall 1999.

**Recommendation No. 4b:** Develop and distribute a sponsors' handbook for administrative management of the CACFP that incorporates all Federal regulations controlling sponsorship of the program and that identifies the costs that are allowable for travel, car leasing, and employee benefit packages.

**FNS Response to Recommendation No. 4b:** FNS will consolidate and update existing Program guidance in the Winter 2000.

**Recommendation No. 4c:** Issue guidance on a required ratio of monitors to homes or increase the number of annual visits which must be made to homes and centers.

**FNS Response to Recommendation No. 4c:** A proposed integrity rule to be published in the Fall 1999.

**Recommendation No. 5a:** Propose regulatory changes to require all sponsors to provide to their State CACFP agencies, and to FNS for monitoring purposes, a listing of all their providers claiming CACFP eligibility for their children based on FSP participation. This information should be readily available from the sponsors. SAs should then be required to provide this information to their State FSP agency.

**Recommendation No. 5b:** Require the State FSP agency to verify all day care income that is or is not reported for food stamp eligibility. This could be part of the normal FSP verification process.

**FNS Response to Recommendation Nos. 5a and 5b:** This recommendation will require additional discussion with OIG and with Food Stamp Program administrators, and may require legislative action as well.

**Recommendation No. 6a:** Instruct FNS to issue guidance so that the recovery of ineligible program funds from sponsors comes from the entities which are directly responsible for the ineligible amounts being claimed. Ineligible provider payments should come from the providers at fault. Ineligible sponsor payments should come from the sponsor.

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## **EXHIBIT E - FOOD AND NUTRITION SERVICE'S WRITTEN RESPONSE TO THE DRAFT REPORT**

**Recommendation No. 6b:** Instruct FNS to ask other States how they collect CACFP claims against sponsor/providers, and issue the same guidance to these States, if necessary.

**FNS Response to Recommendation Nos. 6a and 6b:** FNS will continue through the Winter 1999 to explore ways of dealing with this concern with OIG, OGC, and State agency administrators.

**Recommendation No. 7:** Instruct the SAs to provide some mechanism to inform parents of the participation of their day care providers in the CACFP and encourage their awareness of the activities of those providers.

**FNS Response to Recommendation No. 7:** FNS will address in Program guidance in the Fall 1999.