Department of Health and Human Services

OFFICE OF INSPECTOR GENERAL

STATES' MONITORING OF SUBGRANTEES IN THE FOSTER CARE PROGRAM: A DESCRIPTION OF SIX STATES' SYSTEMS

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A B S T R A C T

As part of a broad Office of Inspector General effort to review the management of grant programs under the Department of Health and Human Services, this report describes States' program and fiscal oversight of subgrantees in the Title IV-E foster care program. This is a companion report to "Oversight of States' Subgrantee Monitoring in the Foster Care Program" (OEI-05-03-00060), which reported that monitoring systems in three of the six States are inadequate.

For this inspection, we interviewed staff and reviewed monitoring protocols and subgrantee files in six States that administer over 45 percent of the $5 billion that the Administration for Children and Families (ACF) awards annually for the foster care program. In all six States, we found that program monitoring typically consists of an onsite visit to subgrantees, and fiscal monitoring typically consists of an independent audit. In some States these monitoring mechanisms are minimal or not implemented as intended. In addition, all six States rely on rate setting to manage foster care expenditures.

Given the extent that States appear to be using subgrantees to carry out fundamental foster care services, lax monitoring can have a significant impact. States with limited monitoring systems may want to consider bolstering their program and fiscal monitoring. The ACF could consider assisting States in their efforts by providing expertise and guidance on subgrantee monitoring, and facilitating communication among States. We hope the information in this report will be helpful in developing this assistance and guidance.

OBJECTIVE

To describe selected States' program and fiscal oversight of subgrantees in the foster care program.

BACKGROUND

The Administration for Children and Families (ACF) awards approximately $5 billion each fiscal year to States that serve about 800,000 children in the Federal Title IV-E foster care program. Most States award some portion of their Federal foster care grant to subgrantees to provide core program services, such as child placement and residential care.

According to Federal grants management requirements under 45 CFR Part 74, States must oversee subgrantees to ensure that subgrantees comply with Federal fiscal and program regulations, use funds for authorized purposes, and achieve performance goals. The ACF must ensure that States administer their foster care programs in accordance with Federal regulations.

We conducted site visits to 6 States representing over 45 percent of Title IV-E spending. We interviewed monitoring staff, reviewed relevant monitoring policies and protocols, and reviewed documentation of States' monitoring for 15 to 19 subgrantee files in each State.

This is a companion report to "Oversight of States' Subgrantee Monitoring in the Foster Care Program" (OEI-05-03-00060), which reported that monitoring systems in three of the six selected States are inadequate. That report also found that ACF pays minimal attention to States' subgrantee monitoring and has little information about how States monitor subgrantees. While that report provides an assessment of States' monitoring systems, this report provides descriptive information on how subgrantees are being monitored in our selected States. In doing so, this report seeks to assist ACF and States in addressing the problems identified in the first report. Both reports are part of a broader Office of Inspector General effort to review the management of grant programs under the Department of Health and Human Services (HHS).

PROGRAM OVERSIGHT

In all six States, onsite visits are used to monitor subgrantees. In three States, monitoring mechanisms are not implemented as intended. In all six States, subgrantees' provision of services is primarily evaluated through onsite visits, including licensing visits that focus on compliance with regulations. Monitoring in four States also includes program site visits that focus on quality of services. In three States, onsite monitoring mechanisms are not implemented as intended. In these States, some subgrantees did not receive their routine licensing or program site visits.

Outcomes-based monitoring has surfaced in some monitoring systems. Five of six States demonstrated at least some movement toward an outcomes-based model of monitoring. In these States, the collection of outcomes data has augmented, not replaced, more traditional modes of monitoring. Three of these States make limited use of performance-based contracting, which involves rewarding subgrantees financially for positive outcomes.

FISCAL OVERSIGHT

In all six States, fiscal monitoring is minimal. Most States rely on only one mechanism, typically an independent audit, to monitor subgrantees fiscally. Although three States use the more comprehensive Single Audit as their fiscal monitoring mechanism, two of these States' use of the Single Audit is very limited. In some States, fiscal monitoring mechanisms do not apply to all subgrantees or are not functioning adequately.

In all six States, rate setting is used to manage foster care expenditures. In all six selected States, subgrantees are funded through fixed rates. Setting rates differs considerably by State, with some rate-setting methodologies being far more sophisticated than others. Some vulnerabilities inherent in a rate-setting system may impact monitoring. These vulnerabilities include: (1) rates may be set inaccurately; (2) rate-setting processes do not address excess funds or unallowable costs; and (3) fixed rates of payment may create financial incentives for subgrantees to decrease the quality of their services.

CONCLUSION

In many cases, States' program and fiscal monitoring systems are limited: monitoring either covers a limited number of subgrantees, consists of only one monitoring mechanism, or is not functioning as intended. Without quality monitoring, States and ACF may have little assurance that subgrantees are providing quality services to children in a fiscally responsible manner. States with limited monitoring may want to consider bolstering their systems to ensure that all subgrantees are routinely and comprehensively monitored to ensure a high quality of care and the appropriate expenditure of foster care funds.

We found that some selected States have noteworthy aspects of their subgrantee oversight, including outcomes-based monitoring and sophisticated rate-setting methodologies. States could benefit from learning about well-designed monitoring systems and strategies. The ACF may want to consider assisting States in these efforts by providing guidance and facilitating communication among States on subgrantee monitoring and rate setting.

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INTRODUCTION

OBJECTIVE

To describe selected States' program and fiscal oversight of subgrantees in the foster care program.

BACKGROUND

The Administration for Children and Families (ACF) administers the foster care program, which is authorized under Title IV-E of the Social Security Act and which awards nearly $5 billion each fiscal year in entitlement grants to States that serve about 800,000 children under Title IV-E annually.[1] Most States subaward some portion of their Title IV-E funds to subgrantees[2] to carry out core program activities, such as child placement and residential care.

Recent Federal Interest in Subgrantee Monitoring

In 2001, the Secretary of the Department of Health and Human Services (HHS) created an initiative to improve the management of HHS grant programs. The Office of Inspector General (OIG) has also undertaken a broad effort to review the control, effectiveness, and value of HHS grant programs.

Federal stakeholders, including the Office of Management and Budget (OMB) and Congress, have expressed concern that States are not adequately monitoring their subgrantees, and that this may reflect a lack of Federal agency oversight. Based on this concern, OMB created an interdepartmental Task Force on Subrecipient Monitoring in 2002.[3] This task force is reviewing regulations and policies to identify whether Federal guidance and oversight of subgrantee monitoring is adequate. Congress has also shown its concern by requesting reviews of subgrantee monitoring in other HHS programs.[4]

This is a companion report to "Oversight of States' Subgrantee Monitoring in the Foster Care Program" (OEI-05-03-00060), which found that monitoring systems in three of the six selected States are inadequate. That report also found that ACF pays minimal attention to States' subgrantee monitoring and has little information about how States monitor subgrantees. While that report provides an assessment of States' monitoring systems, this report provides descriptive information on how subgrantees are being monitored in our selected States. In doing so, this report seeks to assist ACF and States in addressing the problems identified in the first report.

Increased Use of Subgrantees in the Foster Care Program

According to a recent study, nearly all States use subgrantees to provide core foster care services to at least some of their foster children.[5] Foster care services provided by subgrantees include child placement services, such as recruiting and training foster families, placing children with specific families, and arranging services for these children while in their placements. Subgrantees may also provide services related to residential care, using professional staff to care for foster children in group homes, residential institutions or schools, mental health or other specialty treatment facilities, and emergency shelters.

The increasing privatization of foster care services has led to concerns about the accountability of subgrantees within the foster care program. Recent State audits have substantiated the need for concern. In 2000, Ohio's State Auditor found that more than $9 million in foster care funds had been misspent by private agencies on housing and automobile leases, private jet fuel, and other unallowable purchases. These audits uncovered "lax control over Federal foster care money, a lack of financial and program monitoring, abuse of public funds, and the compromised care of some children."[6]

Without adequate oversight of foster care subgrantees, the safety and welfare of thousands of children a year are potentially jeopardized and millions of dollars in annual Federal funds are vulnerable to abuse.

States' Monitoring of Subgrantees

In HHS, responsibilities for State administration of Federal grant funds are delineated by two sets of Federal requirements:

- the Uniform Administrative Requirements for Awards and Subawards (45 CFR Part 74),[7] and
- the Single Audit Act (implemented by OMB Circular A-133).

Specifically, 45 CFR Part 74 contains HHS grants management regulations and incorporates OMB Circular A-133 by reference.

These Federal grants management requirements[8] require States to:

- Ensure that subgrantees are complying with program requirements and achieving performance goals.
- Ensure subgrantees are complying with fiscal requirements, such as having appropriate fiscal controls in place, and are using awards for authorized purposes.

States can ensure that subgrantees are meeting these requirements through a variety of mechanisms, including progress reports, site visits, financial reports, independent (third party) financial audits, and/or internal (State-conducted) financial audits.

Under OMB Circular A-133, certain subgrantees must have a specific type of independent audit, called a Single Audit. Single Audits include a traditional financial audit of subgrantees' basic financial statements, as well as an auditor's report on subgrantees' internal controls and an opinion on subgrantees' compliance with requirements of major Federal programs.

Subgrantees exempt from the Single Audit include: all for-profit subgrantees, and non-profit subgrantees receiving less than $500,000 in total Federal awards, and "vendors." States use Federal guidelines delineated in OMB Circular A-133, §__.210 to determine whether subgrantees are "subrecipients" and thus subject to a Single Audit, or "vendors" and not subject to a Single Audit.

These guidelines characterize "subrecipients" as subgrantees who carry out the program: they may determine eligibility, make programmatic decisions, have their performance judged against the program objectives, and they must comply with program requirements. "Vendors" are characterized as subgrantees who provide goods and services that are ancillary to the operation of the program: they provide goods and services within normal business hours to many different purchasers, operate in a competitive environment, and are not subject to program compliance requirements. The guidelines direct States to use their judgment in making this determination. We found that some States considered foster care subgrantees to be "subrecipients," and other States considered subgrantees providing the same core services to be "vendors."

SCOPE

The intent of this report is to provide descriptive information regarding monitoring of subgrantees who provide child placement services or residential care in six States. This report does not attempt to assess whether monitoring mechanisms include appropriate measures or cover appropriate issues. Nor does it assess subgrantees' fiscal and program performance. Finally, it does not examine subgrantees that provide only training, adoption, or independent living services under the Title IV-E program.

METHODOLOGY

We reviewed six States' program and fiscal oversight of foster care subgrantees through onsite interviews with State and county monitoring staff, a review of monitoring protocols and tools, and a review of subgrantee monitoring files.

Our States included Texas, Michigan, Massachusetts, North Carolina, Pennsylvania, and California. In four of the States, the foster care program was directly administered by the State. In two of the States, the program was jointly administered by the State and the counties. In these States, we selected the two counties serving the largest number of Title IV-E children for our review.

Overall, the 6 States comprise more than 45 percent of the Federal fiscal year (FY) 2002 Title IV-E funds and are located in 6 of the 10 ACF regions. The States and counties we selected funded more than 1,500 foster care subgrantees during their most recent fiscal year.

For a further discussion of our selection of States and subgrantees, please see Appendix A.

Staff Interviews. To understand the complexities of State and county monitoring systems, we conducted onsite interviews with staff responsible for monitoring subgrantees. Typically, this included interviews with program, fiscal, and licensing staff. In county-administered States, we interviewed State and county staff responsible for monitoring subgrantees in our selected counties.

We used structured interview guides to collect information about State and county monitoring of subgrantees, focusing in-depth on each monitoring mechanism. We also used these interviews to gather information about other State and county processes, including monitoring of outcomes, use of performance-based contracting, and monitoring of costs and payments through rate setting and cost-based reimbursement. We supplemented our interviews with a review of monitoring policies, protocols, and guidance.

Subgrantee File Review. To assess whether or not State and county monitoring systems were functioning as intended, we selected and reviewed 15 to 19 subgrantees in each State from State FY 2003. In the county-run States, we selected 8 subgrantees from each selected county, for a total of 16 subgrantees in the State. To represent the various types of subgrantees, we selected both low- and high-volume child placement agencies, as well as low- and high-volume residential care facilities in each State or county. Overall, we reviewed files for 98 subgrantees.

For our file review, we used a structured data collection instrument to examine evidence of monitoring, such as site visit reports, audit reports, financial reports, and licensing reports. We did not examine evidence of rate setting or focus on outcomes or performance-based contracting in our review of subgrantee files.

Limitations of Data

Because we did not randomly select States, our findings cannot be projected to the larger universe of States. They do, however, reflect subgrantee monitoring in States that account for over 45 percent of the Title IV-E foster care funds.

This inspection was conducted in accordance with the *Quality Standards for Inspections* issued by the President's Council on Integrity and Efficiency.

In all six States, onsite visits are used to monitor subgrantees. In three States, monitoring mechanisms are not implemented as intended.

In all six selected States, subgrantees' provision of services is primarily evaluated through onsite visits. In three States, these monitoring mechanisms are not operating as intended.

Onsite foster care licensing visits and program site visits are the primary mechanisms used to monitor subgrantees.

All six selected States rely on onsite monitoring to oversee subgrantees' provision of services. Onsite monitoring may include case file reviews, interviews with children and staff, a review of staff training and qualifications, and observation of the condition and appropriateness of the facility.

Table 1: Types of Program Monitoring Mechanisms Used in Six States

	State A	State B	State C	State D	State E	State F
Licensing Visits	X	X	X	X	X	X
Comprehensive Program Site Visits		X	X		X	X
Targeted Program Site Visits			X			X

Source: OEI State Site Visit Data

In all six States, monitoring includes licensing site visits. As seen in Table 1, all six of our selected States use routine licensing visits to monitor foster care subgrantees. Subgrantees are licensed annually in three States, and every 2 years in the other three States. Licensing is fairly similar across States; visits focus on compliance with regulations, and are usually conducted by a State licensing department separate from the foster care department. Licensing site visits may include assessing compliance with regulations related to safety and protection of civil rights, as well as a review of numerous program issues, such as case record documentation, service planning process, health and treatment services, and discipline.

In four States, monitoring also includes program site visits. In addition to licensing visits, comprehensive program site visits are used in four States to ensure program accountability. In two of these States, subgrantees receive more than one type of program site visit. They receive both a comprehensive program visit and a more targeted program site visit. These targeted visits review such things as service utilization and outcomes or are geared toward identifying issues in need of technical assistance. (See Table 1.)

While comprehensive program site visits and licensing site visits are generally similar in that they both tend to use the same methods (policy and record reviews, interviews, and observation) and have some overlap in content, there are some key distinctions. The purpose of licensing site visits is to assess compliance with laws and regulations, while the purpose of program site visits is to ensure that children receive quality services. Program site visits may also include a technical assistance component. Further, in county-administered States, such as State C and State E, licensing visits are conducted by State staff and cover subgrantees across the State, and program site visits are conducted by county staff and may vary by county.

Monitoring staff in licensing and program departments in four States reported that they communicate with each other and coordinate their monitoring efforts to some extent. In a fifth State, staff indicated that program and licensing departments do not coordinate and cited this lack of coordination as one of the barriers they face in trying to monitor subgrantees effectively.

In three States, program or licensing visits are conducted less frequently than annually. Three States' onsite visits are conducted at least annually; however, visits in the remaining three States are less frequent. State B only requires licensing visits to its subgrantees every 2 years and program site visits every 12 to 18 months. In State D, all subgrantees receive one licensing visit every other year and no program site visit. Program monitoring staff in this State rely heavily on a network of State and local oversight entities to provide referrals for any programmatic problems, rather than establishing regular program site visits. In State A, most subgrantees are licensed only once every 2 years. Some subgrantees in this State receive licensing site visits, but for some subgrantees, their biennial licensing only consists of a desk review of submitted materials.

In three States, onsite monitoring mechanisms are not implemented as intended.

In three States, licensing or program monitoring is not implemented as intended. For example, in State C, licensing is designed to include annual site visits for all subgrantees, but less than half of the selected subgrantees actually received this annual licensing visit. In one county in this State, licensing is the only program monitoring mechanism for nearly all child placement agencies. In this county, half of the subgrantees we reviewed did not receive a site visit and thus had not been relicensed, resulting in foster children being cared for by unlicensed providers. State licensing staff indicate that they have limited resources and thus give priority to investigating complaints or problems over conducting their annual licensing visits.

Program monitoring is not implemented as intended in State B, where staff were unable to provide documentation of program visits for more than half of the subgrantees selected. This State also indicated that they lack resources and have lost significant staff recently.

Finally, our review found that one county in State E did not meet its' own program site visit goals, although county staff actually visited all selected subgrantees at least annually. County staff intended to visit all subgrantees quarterly; however, we found that only half of the selected subgrantees were visited quarterly.

Outcomes-based monitoring has surfaced in some monitoring systems.

Five of the six selected States demonstrated at least some movement toward an outcomes-based model of monitoring. In each of these States, the collection of outcomes data has augmented, not replaced, more traditional monitoring mechanisms, such as site visits. Traditionally, States have paid subgrantees based on the services they provide and have monitored their processes. In an outcomes-based system, States monitor the outcomes of these processes. Thus, States encourage subgrantees to focus more on outcomes and less on processes. States may take additional steps to reinforce a focus on outcomes by offering incentive payments for positive performance or structuring reimbursement around performance, as in performance-based contracting.

In three States, performance-based contracting is used on a limited basis. In all three States, subgrantees under these contracts are paid a relatively low monthly fee per foster child, with the understanding that they will receive additional funding once they meet specified performance outcomes. These outcomes may include successfully transitioning clients to a less restrictive level of care, sustaining a child in a placement for a certain length of time, and successfully moving a child into adoption. Subgrantees under performance-based contracts are typically penalized for negative outcomes, namely when a foster child is returned to the system from an unsuccessful placement. In this situation, the subgrantee shoulders the burden of finding an alternate placement for the child without any additional monthly payments from the State.

In three States, monitoring staff have started to collect outcomes but do not use or analyze the information they collect. For instance, State F determines the number of positive and negative outcomes each subgrantee has per year. State F plans to expand the number and types of outcomes it collects and move to a performance-based contracting system by FY 2006. State D uses performance-based contracting for some subgrantees and has started to collect outcomes for all others, but does not plan to use them until the next contract cycle. In addition, one county in State C collects specific outcomes information related to education and independent living skills. The county does not currently have plans to hold subgrantees accountable for their outcomes.

In all six States, fiscal monitoring is minimal.

In five selected States, fiscal monitoring consists of only one primary mechanism. In four States, an annual independent audit is the only systemic means of monitoring the fiscal functioning of their subgrantees. A fifth State minimally supplements its annual independent audits with additional internal financial audits of approximately 10 residential care facilities each year. Finally, a sixth State's fiscal monitoring consists of an annual review of subgrantees' financial information, such as financial statements, billings and budgets, and an onsite review of selected financial records for some subgrantees.

Of the five States that rely on independent audits, two States use a traditional fiscal audit as opposed to the more comprehensive Single Audit. These States have classified their foster care subgrantees as "vendors," which exempts them from Single Audit requirements. By not employing the Single Audit, these States limit their financial oversight of Title IV-E funds to a review of the basic financial controls of the subgrantee provided by a financial audit. States are not provided with the more specific review of subgrantees' use of program funds that would be conducted in a Single Audit.

Three States use the Single Audit to monitor subgrantees fiscally; however, two States' use of the Single Audit is very limited. State B only requires that a Single Audit be performed on subgrantees for their first year providing services.[9] Of the 19 subgrantees we reviewed from this State, the Single Audit was only required for 4 subgrantees. State D does not correctly identify the grant as Title IV-E funds. Instead, it identifies foster care funds as Social Services Block Grant funds. Because of this error, auditors review the subgrantee's compliance with Social Services Block Grant requirements and not Title IV-E requirements. Only State E uses the Single Audit for all subgrantees and for Title IV-E funds. Both State D and one county in State E supplement the Single Audit by requiring additional auditor opinions and subgrantee financial statements.

In some States, fiscal monitoring mechanisms do not apply to all subgrantees or are not functioning as intended.

Two States' fiscal monitoring abilities are limited due to the fact that they do not require an audit or onsite fiscal review of all of their subgrantees. In one State, subgrantees providing mental health services are not subject to an audit or any other fiscal review related to their Title IV-E funds. Of the 16 subgrantee files we reviewed in this State, 6 subgrantees were not required to submit audits. In the other State, whether or not a subgrantee's finances are reviewed onsite and the extent of that review is based on an assessment of the subgrantee's risk. All high- and medium-risk subgrantees receive a site visit, while 2 percent of low-risk subgrantees are selected for a site visit. All other subgrantees receive a desk review of submitted financial information. Of the 16 subgrantees that we selected, 6 subgrantees did not receive an onsite fiscal review.

We also found that two States' fiscal monitoring is not functioning as intended. In one State, we found that many selected subgrantee files did not include an audit. Further, staff in both of these States perform only a cursory review of submitted audits, limiting the usefulness of the audit as an oversight mechanism. One State has program staff review the audit to make sure "the numbers make sense," even though the staff have not received any financial training. Our review of 16 subgrantee files in this State found no evidence that audits had been reviewed even minimally. The other State only reviews audits to detect severe problems with a subgrantee, such as bankruptcy.

Staffing and resources are not being invested in fiscal oversight.
In the face of States' budget crises, States have drastically reduced fiscal monitoring staff. Four States reported severe limitations in fiscal monitoring due to lack of staff.

Internal audit departments have been especially affected by budget cuts. One State completely cut its internal audit division due to budget issues. Audit offices in three States have only enough resources to perform internal audits in response to complaints or problems, but not enough resources to proactively monitor subgrantees. Funding cuts in two States have left audit divisions without enough staff to provide even reactive internal audits for the Title IV-E program.

In all six States, rate setting is used to manage foster care expenditures.

One way States can manage their foster care expenditures is to use rate setting to establish reasonable rates of payment for subgrantees. Another way States can manage their expenditures is through a cost-based system of reimbursement. Under this system, States reimburse each subgrantee for their actual costs based on itemized invoices that subgrantees submit to the State.

In all six of our selected States, the majority of subgrantees are funded through a rate-setting system of payment rather than a cost-based system of reimbursement. Two of the six States also use a cost-based system of reimbursement for a small minority of their subgrantees. These States use cost-based reimbursement in cases where it is particularly difficult to establish rates, such as for new subgrantees, subgrantees providing new services, or for services with unpredictable costs.

Under a rate-setting system, the State pays subgrantees based on a specific rate they have established prior to the award period, rather than retrospectively reimbursing them based on subgrantees' reported expenses. The State typically determines a per diem/per child rate for the package of services subgrantees will be contracted to provide. For example, the State's rate for residential facilities would encompass the expenses associated with shelter, food, and administrative overhead. To pay a particular subgrantee, the State would multiply this set rate by the number of children served and by the number of days for which care was provided.

Rate-setting processes vary by State, but are used to manage foster care expenditures.

While the rate-setting process differs considerably by State, the goal is the same: to establish a fair, but economical payment that only reflects allowable Title IV-E costs. Rate-setting systems in the six selected States appear to vary along a continuum in their level of sophistication.

At one end of the spectrum are certain rates set using only the most minimal data. In one of the selected States, rates for certain subgrantees are based solely on the amount of funding the State has available. This State does not take into account the costs associated with caring for children in foster care when setting these rates. In another State, rates for certain subgrantees are based solely on childcare costs as reported by the U. S. Department of Agriculture. However, both of these States use more complex methodologies for setting other rates; for example, rates for subgrantees serving children whose needs require advanced levels of care.

At the other end of the spectrum are certain rates set using sophisticated approaches. Three of the selected States base their rates on more complex estimations of actual cost. States review annual or biennial cost reports submitted by their subgrantees. These reports itemize foster care and administrative costs in great detail. In addition, some States require supplemental documentation, such as independent audit statements and time studies assessing staff time spent on allowable foster care activities.

Once States estimate costs, three States establish a general set of rates for all subgrantees based on the intensity of care provided by the subgrantee or the age of the child. Alternately, rates in two States are set for each individual subgrantee.

In several States, final rates are determined by cost and budget considerations and may not reflect subgrantees' estimated expenses. For instance, one State imposes a cap on individual rates that no individual facility rate may exceed, regardless of its expenses. Another State requires new subgrantees to estimate costs up front in order to set a rate. The subgrantee is held to that rate, even if its actual expenses exceed the estimated rate. Finally, in three of the six States, the State legislature makes the final rate determination based on the State's available funding.

The rate-setting process may present vulnerabilities.

While all six States have a significant interest in establishing accurate rates and some dedicate significant resources to doing so, vulnerabilities may still exist.

Rates may be set inaccurately. When States attempt to estimate subgrantees' expenses to provide a basis for the State rate, they run the risk that cost reports do not accurately reflect reasonable, actual costs. For instance, cost reports may be falsified or enhanced by subgrantees seeking to hide unallowable costs or excess funds. Cost reports could also reflect unreasonable costs spent by subgrantees who are poor fiscal managers or subgrantees who failed to obtain a fair purchase price for goods or services, paying more than necessary.

Although States typically use cost estimates to develop rates, it can be difficult to ensure that the rates set by States appropriately reflect accurate, reasonable expenses. One reason for this is that costs are likely to vary across subgrantees. Larger subgrantees may be better able to reduce costs by purchasing in large quantities than small subgrantees. Subgrantees in urban areas may pay considerably higher fixed costs than subgrantees in rural areas. Further, external factors, such as State budget shortfalls and limits imposed by State legislatures, may require that rate-setting staff impose arbitrary caps on rates, thus overriding efforts to reflect reasonable, allowable costs in their rates.

To mitigate some of these vulnerabilities, some of the six selected States use traditional fiscal monitoring mechanisms as part of their rate-setting processes. For instance, two States use audits to ensure the accuracy of cost reports. One of these audits verifies cost report data line item by line item.

Rate setting does not typically address excess funds and/or unallowable costs. While rate setting is used to ensure that rates are reasonable, and therefore, grant funds are expended economically, it does not function to ensure that funds are actually expended only for reasonable and allowable costs. Subgrantees could potentially spend funds on items or services that are unallowable under Title IV-E statute or other Federal regulations. Further, Federal grants management regulations prohibit profit,[10] yet subgrantees may receive excess funding if rates exceed subgrantees' actual costs. This may be unavoidable when paying various subgrantees the same rate, since some subgrantees' costs are likely to exceed the rate, while others' costs are likely to fall short of the rate.

Despite this potential vulnerability, three of our six States' rate-setting processes are not designed to recoup inappropriately spent or excess funds. If these States identify that subgrantees have received excess funds, the only action they take is to readjust the rate during the next cycle of rate setting. Even when States specifically identify subgrantees that did not provide services commensurate with their established rates, States typically do not recoup excess funds; they simply adjust the rate when problems are discovered.

In three States, rate setting includes a mechanism designed to recoup funds; however, only one county in one of these States has a mechanism that applies to more than a small subset of subgrantees. This county requires subgrantees to submit an auditor's statement calculating the amount by which funding exceeded or fell short of subgrantees' expenditures. If auditors identify excess funds, county fiscal staff can require subgrantees to repay this amount. Two other States have some mechanism for recoupment, but only for subgrantees in the first year of a new contract, or for a small sample of subgrantees selected for a targeted audit each year.

While the extent of this vulnerability is unknown, subgrantees in at least three States have been identified as using foster care funds inappropriately. In two of the six selected States, anonymous allegations of misspending led States to discover that some subgrantees spent hundreds of thousands of dollars on items that were unallowable under State and Federal regulations. In addition to these cases, in 2000, the Ohio Auditor of State found that more than $9 million in foster care funds had been misspent by private agencies on housing and automobile leases, private jet fuel, and other egregious purchases. Notably, these abuses of funds were discovered through special inquiries, not through the States' rate-setting process or routine fiscal monitoring tools.

Rate setting may impact the quality of foster care services. One vulnerability inherent in a rate-setting system is a reduction in the quality of foster care services. Because subgrantees are reimbursed based on the number of children they serve and not on the amount of resources they expend, there is a financial incentive for subgrantees to serve the greatest number of children for the least amount of money. In addition, if States establish rates that are too low, subgrantees may legitimately not have enough money to provide children with quality services. To mitigate this vulnerability, States must rely on program monitoring to ensure that subgrantees are providing quality services at a level commensurate with their assigned rate.

Staff in two States mentioned the impact poor fiscal performance could have on the quality of services. For example, staff in one county identified a situation where children were missing crucial appointments, such as court and doctor visits, because the facility's van broke down, and there were no funds available to repair it.

CONCLUSION

In some States, program and fiscal monitoring is limited. In these cases, monitoring either covers a limited number of subgrantees, consists of only one monitoring mechanism, or isn't functioning as intended. Without quality monitoring, States and ACF have no assurance that subgrantees are providing appropriate, quality services to children in a fiscally responsible manner. The States and counties we selected funded more than 1,500 foster care subgrantees in their most recent fiscal year. Given the extent that subgrantees are used to carry out fundamental foster care services, lax monitoring can have a significant impact.

To improve their oversight of subgrantees, States with limited monitoring could bolster their program and fiscal monitoring mechanisms by ensuring that all subgrantees are routinely and comprehensively monitored to ensure a high quality of care and the appropriate expenditure of foster care funds. Additionally, these States could add a means to recoup funds to their current rate-setting systems to address any subgrantees that use Federal funds for unallowable costs or retain excess funds.

States could benefit from learning about each other's monitoring systems and oversight strategies. We found that some States have noteworthy aspects within their subgrantee oversight systems. Some States have sophisticated program-monitoring mechanisms that include outcomes-based monitoring through performance-based contracting. Also, some States combine intricate rate-setting methodologies with traditional fiscal-monitoring mechanisms to reduce vulnerabilities inherent in the rate-setting process.

We encourage ACF to assist States by providing guidance and facilitating communication between States on subgrantee monitoring and rate setting. Further information and guidance on good rate setting and subgrantee monitoring practices would provide much needed direction to struggling States. We encourage ACF to consider developing expertise at the regional level on these practices, particularly those related to outcomes monitoring, including performance-based contracting, and rate setting. Further, ACF could consider holding regional or interregional conference calls to discuss existing and emerging practices, and encouraging States to utilize

National Resource Centers, such as the Center on Organizational Improvement, for technical assistance.

METHODOLOGY: SELECTION OF STATES AND SUBGRANTEES

To understand States' monitoring of subgrantees we conducted site visits in six States. This appendix provides greater detail regarding our selection of States and subgrantees.

State Selection

We selected the six study States based on the following factors: (1) maximizing coverage of Title IV-E funds; (2) representing both State-administered and county-administered States; (3) maximizing coverage of ACF regions; and (4) avoiding States participating in Child and Family Services Reviews or in the OIG region VII's case study of eight States' foster care programs. In our final selection of States, we included 3 of the 11 States that have a county-administered system.

Our six States include three State-administered systems: Texas, Michigan, and Massachusetts; and three county-administered systems: California, Pennsylvania, and North Carolina. In our county-administered States, we selected the two largest counties based on the number of Title IV-E children served. In California, we selected Los Angeles and San Diego counties, and in Pennsylvania, we selected Philadelphia and Allegheny counties. We did not select any counties in North Carolina due to the State's exclusive role in monitoring subgrantees. Even though the counties in North Carolina are responsible for administering the foster care program, they are not responsible for monitoring the foster care subgrantees.

Subgrantee Selection

Due to the intensity of our case file review, we limited the number of subgrantee files selected. We estimated that we could complete between 15 to 20 case file reviews in each State. We used the following procedure to ensure that our selection of subgrantees included representation of both child placement agencies and residential facilities, and included subgrantees that served a high volume of Title IV-E children, as well as those that served a low volume of Title IV-E children. Our pre-inspection research indicated that States' monitoring practices might vary between these different types of subgrantees.

From each State and county selected, we requested a list of all foster care subgrantees providing child placement or residential care to Title IV-E children in State FY 2003. To select subgrantees we stratified each subgrantee list, first by type of subgrantee (i.e., child placement agencies and residential facilities) and then by the number of Title IV-E children served. To stratify by number of children served, we calculated the average number of children served, and then designated subgrantees as low or high volume, according to where they fell in relation to the average. We then randomly selected subgrantees from each of the four groups: low-volume child placement agencies, high-volume child placement agencies, low-volume residential facilities, and high-volume residential facilities.

In each State we randomly selected 16 foster care subgrantees. In county-run States, we randomly selected eight subgrantee files in each of the two selected counties. In State D, one subgrantee did not fit our sampling criteria and was discarded in our analysis. In State B, a few selected subgrantees had more than 1 contract with the State, bringing the total number of files reviewed up to 19. (See Table 2.)

Table 2: Sample and Universe of Subgrantees Serving Title IV-E Eligible Children During States' Fiscal Year 2003

State/County	Sample	Universe
State A	16	472
State B	19	132
State C, County 1	8	224
State C, County 2	8	68
State D	15	172
State E, County 1	8	132
State E, County 2	8	49
State F	16	263
Total Subgrantees	98	1,512

Although State D is primarily State-administered, a portion of the foster care program is privately administered. For the purposes of this study, we focused only on the portion of State D's program that is State-administered. State D contracts with subgrantees through a central office and through local offices and regional offices. Our file review included subgrantees hired by all three types of entities. The vast majority of the subgrantees were selected from the State's central office, as this entity has significantly more subgrantees than any of the regional or area offices.

CHARACTERISTICS OF MONITORING SYSTEMS IN SIX STATES

To provide a more complete description of monitoring systems used by each State or county, this appendix describes routine monitoring mechanisms used in each State to ensure program and fiscal integrity. Each table contains three descriptive elements: intended coverage, intended frequency, and actual utilization.

First, *intended coverage* indicates the set of subgrantees for which the mechanism is supposed to be used. In some cases this will be "all," as some mechanisms apply to all subgrantees. However, some States use different monitoring mechanisms for certain subsets of subgrantees depending on subgrantee characteristics, such as type of services provided.

The second column indicates the *intended frequency* at which the monitoring mechanism is supposed to be used.

The *actual utilization* column describes whether the mechanism is meeting its *intended coverage* and *intended frequency* listed in the first two columns. The numerator is the number of selected subgrantees that were actually monitored using the mechanism at the *intended frequency*. The denominator is the number of subgrantees that were intended to be monitored using the mechanism at the *intended frequency*.

> Example:
>
> We selected 16 subgrantees in State X.
>
> *Intended Coverage*: State X intends to conduct program site visits for residential facilities only. We selected eight residential facilities.
>
> *Intended Frequency*: State X intends to conduct program site visits annually.
>
> *Actual Utilization:* Only four residential facilities actually received a site visit annually. Thus, for this mechanism the utilization column would read 4/8. (Four residential facilities actually received a site visit when eight were supposed to receive a site visit.)

An empty space means the State does not use the mechanism.

State A: Characteristics of Program and Fiscal Monitoring Mechanisms

Monitoring Mechanism	Intended Coverage	Intended Frequency	Actual Utilization
Program Monitoring			
Licensing Site Visit	CPA	Every 2 years	8/8
	Non-Mental Health RF	Annual	2/2
Desk Review/Site Visit	Mental Health RF	Every 2 years	6/6
Program Site Visit			
Additional Site Visit			
Fiscal Monitoring			
Single Audit			
Independent Financial Audit	CPA	Every 2 years	8/8
	Non-Mental Health RF	Annual	2/2
Internal Fiscal Review			

CPA=Child Placement Agency

RF=Residential Facility

Total Number of Sampled Subgrantees = 16

Important Characteristics of State A

In State A, monitoring varies depending on subgrantee characteristics. All child placement agencies are monitored by one department. This department also monitors residential facilities with no mental health services. A second department monitors residential facilities with mental health services.

Child placement agencies and non-mental health residential facilities receive regular licensing visits that focus on compliance but also incorporate some program site visit components. These licensing visits are conducted by program monitoring staff. Residential facilities with mental health services receive a licensing site visit initially and then every 2 years receive a desk review to renew their license. The row in the table marked "Desk Review/Site Visit" reflects this.

As evidenced in the table, residential facilities with mental health services do not receive any form of fiscal monitoring for Title IV-E funds. As noted, these same subgrantees do not receive any licensing site visits after the initial visit.

State B: Characteristics of Program and Fiscal Monitoring Mechanisms

Monitoring Mechanism	Intended Coverage	Intended Frequency	Actual Utilization
Program Monitoring			
Licensing Site Visit	All	Every 2 years	17/19
Program Site Visit	All	Every 12-18 months	8/19
Additional Site Visit			
Fiscal Monitoring			
Single Audit	New Subgrantees	Annual	4/4
Independent Financial Audit	Old* Subgrantees	Annual	7/15
Internal Fiscal Review			

* Subgrantees that have received grants from the State for over 1 year.

Total Number of Sampled Subgrantees = 19

Important Characteristics of State B

For their first year of contracting with the State, subgrantees must submit a Single Audit. The State requires independent financial audits of all other subgrantees. State staff set rates for each new subgrantee using the subgrantee's Single Audit. The State legislature has assumed the responsibility of setting any rate increases after the first year. This State also requires Single Audits for a handful of subgrantees whose rates are set by a competitive bidding process. These subgrantees offer certain difficult-to-provide services.

Historically, the annual audit was an integral part of setting the rates the State paid for foster care services. However, ever since the State legislature decided to set State foster care rate increases, the rate-setting office has had little use for the audits. They continue to receive and track the submission of the audits due to historical precedence. They have also maintained the responsibility of reviewing the audits although they only do so to determine if there are basic solvency issues that would warrant contract termination.

Although staff intends to conduct licensing visits every 2 years and program site visits every 12 to 18 months, our review found that not all subgrantees received these visits. The State used to conduct visits annually but has begun to conduct them less frequently due to a reduction in staff.

State C, County 1: Characteristics of Program and Fiscal Monitoring Mechanisms

Monitoring Mechanism	Intended Coverage	Intended Frequency	Actual Utilization
Program Monitoring			
State Licensing Site Visit	All	Annual	3/8
County Program Site Visit	CPA	Full visit - every 3 years Partial visit - annual	4/4
	RF	Annual	4/4
County Additional Site Visit	RF	Quarterly	4/4
Fiscal Monitoring			
Single Audit			
State Independent Financial Audit	All	Annual	8/8
State Internal Fiscal Review	Randomly Selected RF	Annual	0/0

CPA = Child Placement Agencies RF = Residential Facilities Total Number of Sampled Subgrantees = 8

State C, County 2: Characteristics of Program and Fiscal Monitoring Mechanisms

Monitoring Mechanism	Intended Coverage	Intended Frequency	Actual Utilization
Program Monitoring			
State Licensing Site Visit	All	Annual	4/8
County Program Site Visit	Intensive Treatment CPA	Quarterly	1/1
	RF	Annual	4/4
Additional Site Visit			
Fiscal Monitoring			
Single Audit			
State Independent Financial Audit	All	Annual	7/7
State Internal Fiscal Review	Randomly Selected RF	Annual	0/0

CPA = Child Placement Agencies RF = Residential Facilities Total Number of Sampled Subgrantees = 8

Important Characteristics of State C

According to staff in both counties, monitoring resources focus on residential facilities because of the direct, daily contact these facilities have with children in foster care. For County 1, this focus on residential facilities translates into annual comprehensive site visits, as well as quarterly site visits intended to provide both targeted monitoring and technical assistance.

Although this State is county-administered, State staff retain primary responsibility for licensing and fiscal monitoring of all county subgrantees. We found evidence in both counties that State staff were not licensing all subgrantees in a timely manner. The State used independent financial audits to routinely monitor subgrantees' fiscal performance, during the time period we reviewed. In 2003, this State began monitoring subgrantees through Single Audits rather than independent audits. The State also conducts internal fiscal reviews on a small number of randomly selected residential facilities to ensure that services are provided commensurate with their assigned rate.

To supplement these reviews, County 1 conducts targeted fiscal audits on about a dozen poorly performing subgrantees a year. Because this mechanism is only used in response to identified problems, it is not reflected in the chart as one of the county's primary monitoring mechanisms.

State D: Characteristics of Program and Fiscal Monitoring Mechanisms

Monitoring Mechanism	Intended Coverage	Intended Frequency	Actual Utilization
Program Monitoring			
Licensing Site Visit	All	Every 2 years	15/15
Program Site Visit			
Additional Site Visit			
Fiscal Monitoring			
Single Audit			
Independent Financial Audit	All	Annual	14/14
Internal Fiscal Review			

Total Number of Sampled Subgrantees = 15

Important Characteristics of State D

State D's fiscal monitoring includes Single Audits. However, since foster care funds are misidentified as Social Services Block Grant funds, auditors do not review subgrantees' compliance with Title IV-E requirements. Due to this error, these subgrantees' Single Audits do not provide a more comprehensive review of program funds than routine independent fiscal audits would. Thus, the table indicated that subgrantees receive an independent financial audit and not a Single Audit. This State supplements the financial audit by requiring auditors to submit additional schedules and opinions on subgrantees' financial position.

State D's routine program monitoring consists solely of biennial licensing visits. Foster care program monitoring staff in this State rely on a complex network of other oversight entities (such as case workers, licensing staff, and fiscal monitoring staff) for referrals of problems with particular subgrantees.

State E, County 1: Characteristics of Program and Fiscal Monitoring Mechanisms

Monitoring Mechanism	Intended Coverage	Intended Frequency	Actual Utilization
Program Monitoring			
State Licensing Site Visit	All	Annual	8/8
County Program Site Visit	All	Annual	8/8
Additional Site Visit			
County Reports	PBC Subgrantees	Monthly	2/2
County Reports	PBC Subgrantees	Twice a year	2/2
Fiscal Monitoring			
County Single Audit	Subgrantees receiving $300,000 or more in Federal funds	Annual	1/1
County Independent Financial Audit	Subgrantees receiving less than $300,000 in Federal funds	Annual	7/7
Internal Fiscal Review			

PBC Subgrantees = Subgrantees contracting under the County's Performance-Based Contracting System

Total Number of Sampled Subgrantees = 8

State E, County 2: Characteristics of Program and Fiscal Monitoring Mechanisms

Monitoring Mechanism	Intended Coverage	Intended Frequency	Actual Utilization
Program Monitoring			
State Licensing Site Visit	All	Annual	8/8
County Program Site Visit	All	Quarterly	4/8
Additional Site Visit			
Fiscal Monitoring			
County Single Audit	Subgrantees receiving $300,000 or more in Federal funds	Annual	7/7
Independent Financial Audit			
Internal Fiscal Review			

Total Number of Sampled Subgrantees = 8

Important Characteristics of State E

County 1 in State E uses performance-based contracting for child placement agencies that serve more than 50 children. In addition to the county's routine program monitoring, these subgrantees must submit two reports related to their performance-based contracts.

All subgrantees in State E are subject to requirements for Single Audits. According to these requirements, subgrantees receiving less than $300,000 in Federal funds are not required to submit a Single Audit. (Since our review, OMB has raised this threshold to $500,000.) For subgrantees subject to a Single Audit, County 1 requires auditors to submit additional schedules and opinions on subgrantees' financial position. For subgrantees receiving less than $300,000 in Federal funds, County 1 requests that subgrantees submit a traditional independent fiscal audit.

State F: Characteristics of Program and Fiscal Monitoring Mechanisms

Monitoring Mechanism	Intended Coverage	Intended Frequency	Actual Utilization
Program Monitoring			
Licensing Site Visit	All	At least annual	13/16
Desk Review/Site Visit	All	Annual	16/16
Program Site Visit			
Additional Site Visit	All except Emergency Shelters	Annual	15/15
Fiscal Monitoring			
Single Audit			
Independent Financial Audit			
Internal Fiscal Review	All	Annual	16/16

Total Number of Sampled Subgrantees = 16

Important Characteristics of State F

State F has a unique approach to monitoring. The State uses one site visit that incorporates both program monitoring and an internal fiscal review. Also, State F systematically varies its monitoring practices based on an assessment of subgrantee risk. The State uses a risk-based approach for most fiscal and program monitoring and assigns subgrantees a separate risk designation for licensing site visits, program desk review/site visits, and internal fiscal reviews. This State assesses about 100 different factors using three instruments to determine subgrantees' risk designations. These factors range from the subgrantee's level of internal controls to the subgrantee's history of noncompliance with requirements to the experience level of the subgrantee's key management staff. For program desk reviews/site visits, risk factors are weighted according to their relative importance, and subgrantees are assigned risk designations based on the aggregation of weighted risk "points." The frequency and intensity of each monitoring mechanism depends on a subgrantee's risk designation.

While State F utilizes program desk reviews/site visits and internal fiscal reviews at 100 percent, because the State uses a risk-based approach, not all selected subgrantees were actually visited. All selected subgrantees were evaluated, using the risk assessment instruments, to determine whether the subgrantee needed to be visited and the intensity of the monitoring during the visit. For example, the risk assessment determines whether the subgrantee needs to have a program site visit or a desk review. While all subgrantees' risk levels were assessed, 10 subgrantees actually received a program site visit, and 8 actually received a site visit including an internal fiscal review.

All subgrantees, except emergency shelters, also receive an additional site visit. This additional site visit determines the level of care a subgrantee is able to provide. The level of care the subgrantee is authorized to provide dictates the rate it will receive per child.

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END NOTES

[1] According to Administration for Children and Families (ACF) estimates, 810,000 children spent some time in Title IV-E foster care during Federal FY 2002. There were an estimated 534,000 children in Title IV-E foster care on September 30, 2002. Retrieved March 11, 2004 from: www.acf.hhs.gov/programs/cb/dis/afcars/publications/afcars.htm.

[2] We use the term "subgrantee," as opposed to terms that are commonly used by States but have specific technical definitions in Federal grants management requirements, such as "contractor" or "subrecipient."

[3] Task Force members include staff from: the Office of Management and Budget (OMB); the Departments of Health and Human Services (HHS), Transportation, Agriculture, Education, Justice, Labor, and the Navy; the Federal Emergency Management Agency; the National Science Foundation; and the States of Louisiana and Texas.

[4] A 2002 Government Accountability Office (GAO) study, "Welfare Reform: Federal Oversight of State and Local Contracting can be Strengthened," GAO-02-661, 2002, examined State and local agency monitoring of subgrantees receiving Temporary Assistance for Needy Families funds, and found that ACF staff were not aware of monitoring problems identified in States' Single Audit reports. These audit reports cited weaknesses in States' monitoring, including inadequate fiscal and program monitoring of local contracting entities.

Congress has also expressed concern that the Health Resources and Services Administration (HRSA) does not adequately monitor grantees' oversight of their subgrantees. Consequently, in 2001, the Senate Finance Committee requested that the Office of Inspector General (OIG) review HRSA's oversight of Ryan White CARE Act Title I and Title II grantees and grantees' oversight of their subgrantees.

[5] The National Survey of Child and Adolescent Well-Being (NSCAW) found that at least 90 percent of States used subgrantees to provide child placement and residential care that specifically includes treatment. This study did not include other commonly used private residential facilities, such as group homes, residential schools, or

emergency shelters in their survey. Further, there has been little research into the extent to which States use subgrantees: whether States use subgrantees to serve a small subgroup of the State's foster children or for the majority of foster children in the State. The NSCAW reports that 70 percent of States use subgrantees statewide to provide residential treatment services, and an additional 26 percent use subgrantees "in some counties." The NSCAW local agency survey also found that using subgrantees to provide foster care services is more common in urban areas, larger counties, larger agencies, and State-administered foster care systems. Department of Health and Human Services, Administration for Children, Youth, and Families, "National Survey of Child and Adolescent Well-Being: State Child Welfare Agency Survey: Report" and "National Survey of Child and Adolescent Well-Being: Local Child Welfare Agency Survey: Report," Washington, 2001.

[6] "Petro Issues Montgomery County Foster Care Audit," Ohio Auditor of State News Release. February 10, 2000.

[7] There are two sets of HHS regulations that provide Uniform Administrative Requirements: 45 CFR Part 74, which typically applies to awards to nongovernmental entities, and 45 CFR Part 92, which typically applies to awards to governmental entities. Until very recently, States receiving Title IV-E funds were subject to the requirements under 45 CFR Part 74, which are very similar to those under 45 CFR Part 92. Recently, HHS re-designated Title IV-E State grants to be subject to 45 CFR Part 92.

[8] OMB Circular A-133, §__.400(d) states that ". . . a pass-through entity shall perform the following for the Federal awards it makes: . . . (3) Monitor the activities of subrecipients as necessary to ensure that Federal awards are used for authorized purposes in compliance with laws, regulations, and the provisions of contracts or grant agreements and that performance goals are achieved."

[9] This State also requires Single Audits for a handful of subgrantees that have their rates set by competitively bidding to provide certain difficult-to-provide services.

[10] 45 CFR § 74.81.