



STATE OF NORTH CAROLINA

INVESTIGATIVE REPORT

HARNETT COUNTY PARTNERSHIP FOR CHILDREN, INC.

COMMUNITY EDUCATION AND PROGRAMS, INC.

LILLINGTON, NORTH CAROLINA

MAY 2010

OFFICE OF THE STATE AUDITOR

BETH A. WOOD, CPA

STATE AUDITOR

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Office of the State Auditor



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AUDITOR'S TRANSMITTAL

The Honorable Beverly Perdue, Governor
Lanier Cansler, Secretary, North Carolina Department of Health and Human Services
Dr. Deborah Cassidy, Director, North Carolina Department of Health and Human Services,
Division of Child Development
Members of the North Carolina General Assembly
Mr. Ashley Thrift, Chair, Board of Directors, The North Carolina Partnership for Children, Inc.
Ms. Karen Mintz, Chair, Board of Directors, Harnett County Partnership for Children, Inc.

Ladies and Gentlemen:

Pursuant to North Carolina General Statute §147-64.6(c)(16), we have completed an investigation of an allegation regarding the activities of a contractor for the Harnett County Partnership for Children, Inc. The results of our investigation, along with recommendations for corrective action, are contained in this report.

Copies of this report have been provided to the Governor, the Attorney General and other appropriate officials in accordance with G.S. §147-64.6 (c) (12).

Respectfully submitted,

A handwritten signature in cursive script that reads "Beth A. Wood".

Beth A. Wood, CPA
State Auditor

May 25, 2010

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INTRODUCTION

The Office of the State Auditor received a complaint through the *State Auditor's Hotline* alleging the misuse of Smart Start¹ funds paid to Community Education and Programs, Inc. (CEAP), a contractor for the Harnett County Partnership for Children, Inc. (Partnership). The funds were requested by CEAP in order to pay a vendor for the cost of supplies ordered for child care centers in Harnett County. It was also alleged that CEAP may have been selling day care center supplies paid for by the Partnership.

To conduct our investigation of the complaint, we performed the following procedures:

- Examination of relevant documents and records;
- Interviews and correspondence with employees and management of the Harnett County Partnership for Children, Inc., Community Education and Programs, Inc., The North Carolina Partnership for Children, Inc., and numerous day care centers in Harnett County, North Carolina;
- Review of policies and procedures of The North Carolina Partnership for Children and the Harnett County Partnership for Children, Inc.;
- Review of applicable North Carolina General Statutes and North Carolina Administrative Code.

CEAP's executive director's lack of cooperation with us impeded our investigation. CEAP moved from their Lillington facility in June 2009 and subsequent attempts to contact the executive director via phone and e-mail were not met with a response. As a result of the executive director's lack of cooperation, much of the documentation we requested was not provided and a subpoena was served on September 30, 2009. A court order for enforcement of the subpoena was obtained on October 1, 2009. Very limited amounts of additional documentation, as well as some computers, were made available as a result of the court order. Legal action based on this lack of cooperation is pending as of the publication date of this report. The findings in this report will be referred to the following federal and state authorities:

- United States Attorney's Office, Eastern District of North Carolina
- Federal Bureau of Investigation
- Internal Revenue Service
- Office of the Attorney General for the State of North Carolina
- North Carolina State Bureau of Investigation
- North Carolina Department of Revenue
- Office of the District Attorney, Judicial District 11A

This report presents the results of our investigation. The investigation was conducted pursuant to North Carolina General Statute §147-64.6(c)(16) rather than as a financial statement audit or review. An independent public accounting firm performs a financial statement audit of the Partnership on a biennial basis.

¹ Smart Start is a public-private initiative that provides early education funding to every county in North Carolina. Smart Start funds are administered through local nonprofit organizations called Local Partnerships. The Harnett County Partnership for Children, Inc. is one such local partnership. The North Carolina Partnership for Children, Inc. is the statewide nonprofit organization that provides oversight and technical assistance for local partnerships.

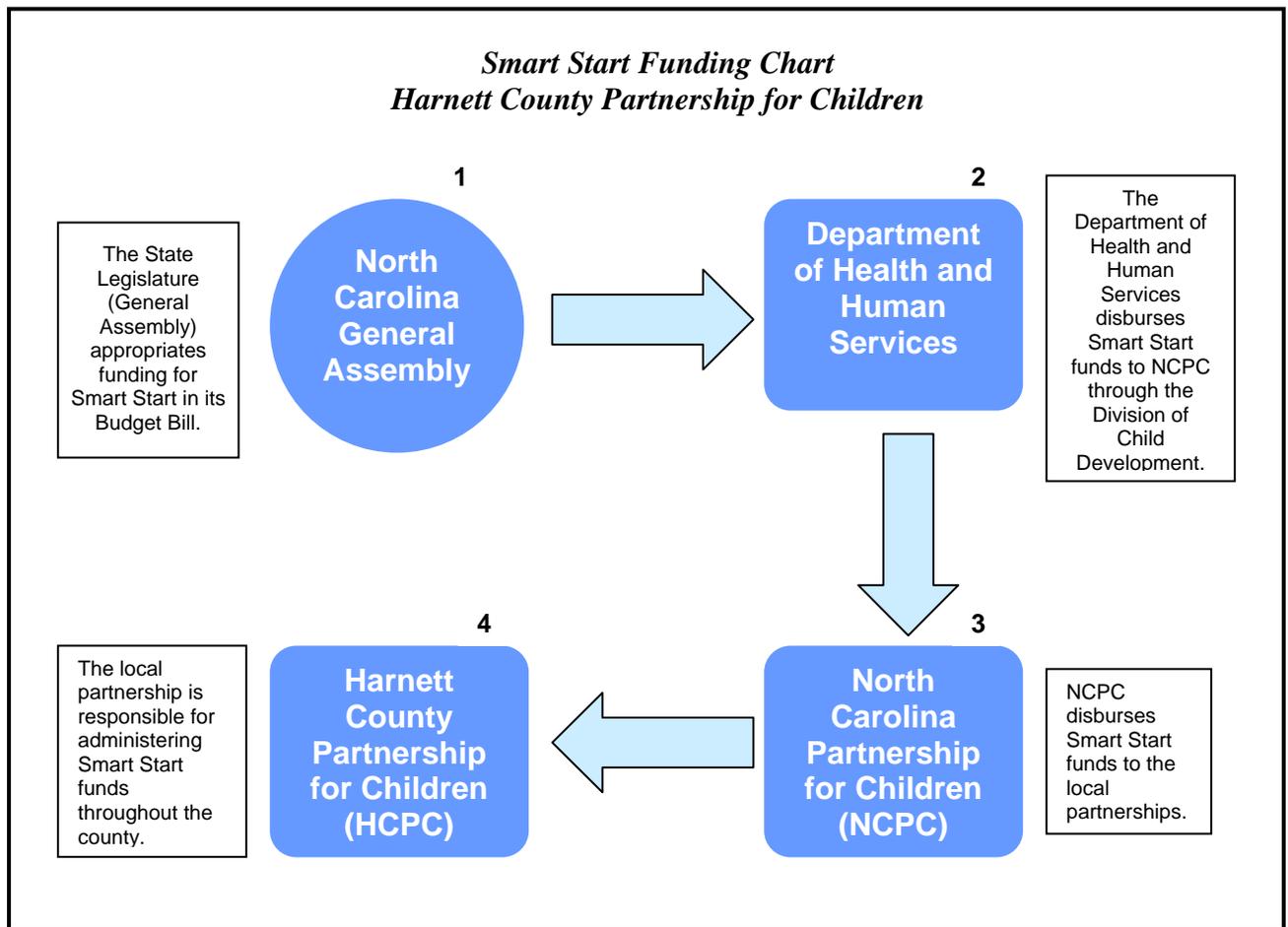
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ORGANIZATION AND PROGRAM OVERVIEW

The Harnett County Partnership for Children, Inc. (Partnership) was incorporated on October 18, 1994 and is organized as a nonprofit corporation under section 501(c)(3) of the Internal Revenue Code.² The Partnership was established to develop and provide early childhood education and developmental services to children and their families in Harnett County.

The Partnership’s major source of revenue is Smart Start funding from the state of North Carolina. (Refer to Figure 1 for funding process.³) The funding is received through The North Carolina Partnership for Children, Inc. (NCPC), a nonprofit corporation established in 1993 to provide statewide oversight of the Smart Start initiative. NCPC provides technical assistance and training for local Smart Start partnerships in the areas of program development, administration, organizational development, communication, fiscal management, technology, contracts management, and fundraising.

Figure 1



² The benefits of having 501(c)(3) status include exemption from federal income tax and eligibility to receive tax-deductible charitable contributions. An IRS determination of 501(c)(3) status is also recognized for other purposes. For example, state officials may grant exemption from state income, sales, and property taxes.

³ Source: Harnett County Partnership for Children. Revised by the NC Office of the State Auditor.

ORGANIZATION AND PROGRAM OVERVIEW (CONTINUED)

The Harnett County Partnership has 19 board members representing business, government, education, churches, nonprofits, communities, human services, agencies, child care providers, and families. The staff consists of eight full-time employees, including an executive director, program manager, and finance manager. Each of these three management positions experienced turnover during the fiscal year ended June 30, 2008.

NCPC contracted with the Partnership to provide nine different types of Smart Start services in Harnett County for the fiscal year ended June 30, 2008. Two of these service types are identified in the contract as Quality Enhancement and Early Childhood Professional Development. As a result of staffing considerations, the Partnership decided to subcontract these two programs and a Request for Proposal (RFP) was issued.

On June 13, 2007, the Partnership's executive committee recommended, and the board of directors approved, resolutions awarding the two contracts to Community Education and Programs, Inc. (CEAP). Both contracts were for a period of one year (ended June 30, 2008) and both were funded entirely with Smart Start funds.

The first contract was for a Quality Enhancement program having a not-to-exceed amount of \$253,537. Under the terms of the Quality Enhancement contract, CEAP was to use Environmental Rating Scales⁴ and trained quality enhancement specialists to provide action plans, mentoring, modeling, training and materials to child care providers in Harnett County. The contract further stipulated that the funding would support one program coordinator and an unspecified number of contracted quality enhancement specialists.

The second contract was for an Early Childhood Professional Development program having a not-to-exceed amount of \$120,724. The terms of the Professional Development contract called for CEAP to provide individualized professional development portfolios for child care providers. The goal was to enhance the professional growth of child care providers and increase their knowledge in the early childhood field. The contract stipulated that funding would support one program coordinator and one contracted professional development counselor.

Aside from a one-time cash advance for start-up funds, CEAP was to receive monthly reimbursements from the Partnership equivalent to their expenditures under each of the two contracts. Reimbursement requests were submitted on a form called a Financial Status Report. The reports were prepared and signed by the executive director of CEAP. Photocopies of paid invoices, register receipts, checks, payroll registers, and other documents were often furnished in support of the expenditures listed on the Financial Status Report. However, there were some significant gaps in the completeness of the supporting documentation provided to the Partnership.

⁴ The Environmental Rating Scales were developed at the Frank Porter Graham Child Development institute at the University of North Carolina. Each one of the scales has items to evaluate: Physical Environment; Basic Care; Curriculum; Interaction; Schedule and Program Structure; and Parent and Staff Education. The statewide program uses the Environment Rating Scales to help child care centers and family child care homes raise their rating under the state's five-star licensing system.

ORGANIZATION AND PROGRAM OVERVIEW (CONCLUDED)

Once received by the Harnett County Partnership, the Financial Status Reports were reviewed and approved by the finance manager and the executive director. An Invoice Payment Request was prepared by the Partnership's fiscal specialist and approved by the finance manager, executive director, and the board chair (if greater than \$25,000). At the completion of this process, a check was provided to CEAP.

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FINDINGS AND RECOMMENDATIONS

1. CEAP FRAUDULENTLY OBTAINED SMART START REIMBURSEMENTS THROUGH VENDOR INVOICING.

CEAP fraudulently obtained \$86,521 of payments from the Harnett County Partnership for Children by providing copies of held vendor checks and fictitious or unpaid invoices with their reimbursement requests.

- The Partnership paid \$45,590 to CEAP for day care center supplies it ordered from the Kaplan Early Learning Company. The supplies were delivered to the day care centers, but CEAP failed to pay the invoices from Kaplan and instead used the funds for other purposes.
- The Partnership paid \$33,016 to CEAP for employee health insurance from Aetna Global Benefits, the international segment of Aetna, Inc. The checks to Aetna were never mailed and the invoices purported to be from Aetna were fictitious. There was never an insurance policy in effect and the reimbursements from the Partnership were used by CEAP for other purposes.
- The Partnership paid \$6,055 to CEAP for contributions to a 403(b) retirement plan for its employees. Again, the checks were never mailed and the invoices purported to be from Norman C. Payne IV, Inc. DBA Payne Insurance were fictitious. There was never a retirement plan in effect and the funds were used by CEAP for other purposes.
- The Partnership paid \$1,860 to CEAP for invoicing from four other vendors. In all four instances, check copies were submitted as proof of payment. However, the checks had never been mailed.

CEAP's misrepresentations to the Partnership may be a violation of North Carolina General Statute §14-100, *Obtaining property by false pretenses*. For the complete text of G.S. §14-100, see Appendix A. A determination as to other potential violations of state or federal statutes will be made by the law enforcement officials included in the introduction to this report.

Payments for Kaplan Invoicing

In February 2008, CEAP requested an advance of \$35,513 from the Harnett County Partnership to pay for supplies ordered from the Kaplan Early Learning Company. The supplies were to be delivered to child care centers in Harnett County under the Quality Enhancement program and it was later confirmed that the supplies were, in fact, received by the day care centers.

The contracts between the Harnett County Partnership and CEAP provided for a *reimbursement* of expenditures made by CEAP, with the exception of a one-time advance payment for start-up costs. The advance for start-up costs was paid to CEAP in July 2007. However, on the Financial Status Report for January 2008, CEAP requested another advance of funds in the amount of \$35,513. The request was supplemented by a letter from CEAP dated February 6, 2008. The letter contained a one line request for "additional funds ... to pay invoices for a materials and supplies order for Centers and

FINDINGS AND RECOMMENDATIONS (CONTINUED)

Homes in the community.” This was followed by a list of CEAP purchase order numbers and corresponding dollar amounts, the names of the child care centers where the supplies were to be delivered, and an expected payment date of February for the invoices to be received from Kaplan. After a review of the purchase orders to Kaplan provided by CEAP, the Partnership reimbursed CEAP for their January 2008 reported expenditures plus an additional \$35,513 for the requested advance. The invoice payment request was signed by the Partnership’s finance manager, executive director, and the board chair.

In April 2009, a representative of Kaplan contacted the Harnett County Partnership to inform them that CEAP had not paid their invoices. The Partnership reviewed their files and found that the invoices claimed to be unpaid by Kaplan matched the invoice numbers shown on the check copies furnished by CEAP as proof of payment. The total amount of all CEAP checks payable to Kaplan for fiscal year ended June 30, 2008 was \$45,590. Of this total, \$35,513 represented the advance to CEAP and the balance of \$10,077 represented reimbursements to CEAP. It was subsequently determined that the checks had never been mailed to Kaplan and that the funds had not been used for their intended purpose.

Payments for Aetna Invoicing

CEAP followed a similar pattern of fraudulently obtaining funds from the Partnership through the presentation of check copies, payable to Aetna, where the actual checks had never been mailed. In this instance, however, the invoice copies presented to the Partnership as proof of payment were also fictitious. These photocopied “invoices” were for employee health, life, dental, disability, and vision insurance coverage. Our review of bank statements again showed that none of the checks had been cashed. Our communications with Aetna provided confirmation that Aetna had never received the checks and that the “invoices” were actually altered benefits statements showing an account number for Simcom International, a Florida corporation. Aetna further confirmed that they had no record of Community Education and Programs, Inc. or any of the CEAP employee names appearing on these “invoices.”

Payments for Payne Insurance Invoicing

The invoices from Payne Insurance were also fictitious. And once again, copies of checks payable to Payne were submitted by CEAP to the Partnership in support of their reimbursement requests. And again, the actual checks were never mailed. The “invoices” were photocopies that were submitted as CEAP contributions to a 403(b) retirement plan for some of its employees. After reviewing the invoice copies, the vice-president of Payne Insurance indicated that the invoice copies were fabricated and that they did not have a *Payne Financial Management Services Company* as was shown at the top of each invoice copy. She also confirmed that none of the checks had been received by Payne.

Payments for Other Invoicing

Funds were fraudulently obtained from the Partnership for checks written, but never sent, to four other vendors. One check was for a \$500 invoice for training. The other checks and related invoices totaling \$1,360 were for day care center and office supplies.

FINDINGS AND RECOMMENDATIONS (CONTINUED)

RECOMMENDATION

- The Partnership should not make cash advances to contractors unless specifically required to do so under the terms of the contract. The Partnership's board of directors should carefully evaluate all contractor requests for cash advances. Additionally, the board should amend the contract if it elects to make an advance that is outside the terms of the existing contract.
- The Partnership should only accept original invoices (no photocopies) as proof of payment. Invoices that appear questionable in any manner should be supported by a canceled check and a debit entry on the bank statement. Independent verification by the vendor of receipt of payment would also be advisable if the dollar amount is sufficiently large.

2. CEAP FRAUDULENTLY OBTAINED PAYROLL TAX REIMBURSEMENTS.

CEAP fraudulently obtained \$41,040 of payments from the Harnett County Partnership for Children for the reimbursement of payroll taxes. CEAP submitted payroll journals with their reimbursement requests indicating that employee payroll tax withholdings plus the employer's share of Social Security, Medicare, and Federal Unemployment Tax Act (FUTA) taxes had been paid. Specifically, the Partnership paid \$27,162 to CEAP for taxes withheld from employee paychecks and an additional \$13,878 for matching employer contributions (Social Security and Medicare) and the FUTA tax obligation. These taxes were never remitted to tax authorities and the reimbursements were instead used for other purposes.

The contracts between CEAP and the Partnership specified that CEAP was to be reimbursed for expenditures under the cash basis of accounting.⁵ This meant that expenses should have been paid by CEAP before submission to the Partnership for reimbursement. At the time that CEAP paid the net amount of payroll to its employees, it was entitled to receive reimbursement only for that net amount. Once payroll tax withholdings and the employer's share of payroll taxes were remitted to the proper tax authorities, CEAP would then be eligible to submit payment documentation so that they could receive reimbursement for those taxes.

There are very specific rules governing the withholding and payment of payroll taxes. An employer is required to withhold federal income tax, Social Security, and Medicare taxes from employees in accordance with Internal Revenue Code (IRC) §§3102 and 3402. In addition, the employer is required to pay Social Security and Medicare taxes equivalent to the amount withheld from the employee under IRC §3111. The employer is also required to pay Federal Unemployment Tax Act taxes on the employees wages pursuant to IRC §3301. The failure of CEAP to pay these taxes could subject them to penalties under IRC sections including, but not limited to, IRC §§6656, 6672 and 7202.

⁵ Accounting method in which income is recorded when cash is received, and expenses are recorded when cash is paid out.

FINDINGS AND RECOMMENDATIONS (CONTINUED)

In addition to the federal taxes, an employer in North Carolina is required to withhold state income taxes from employees in accordance with G.S. §105-163.2. The taxes are to be paid in accordance with G.S. §105-163.6. The failure of CEAP to pay these taxes could subject them to penalties under G.S. §105-236.

CEAP's misrepresentations to the Partnership for the purpose of obtaining reimbursement of these taxes may also be a violation of G.S. §14-100. For the complete text of G.S. §14-100, see Appendix A. A determination as to other potential violations of state or federal statutes will be made by the law enforcement officials included in the introduction to this report.

RECOMMENDATION

The Partnership should require the contractor to provide documentation which is sufficient to substantiate the amount of the payroll tax liability and proof of payment. This would necessitate that the contractor provide the Partnership with documentation such as payroll registers, canceled checks, bank statements, bank-validated tax payment coupons or EFT (Electronic Funds Transfer) acknowledgment numbers in support of payroll tax deposits. Payroll tax filings (e.g., IRS Form 941) should also be reviewed to determine that reimbursed wages and tax payments equal the amounts remitted to tax authorities.

3. CEAP OBTAINED SMART START REIMBURSEMENTS FOR PAYROLL EXPENSES THAT WERE UNDOCUMENTED OR UNRELATED TO THEIR CONTRACTS.

We found other payroll reimbursement deficiencies totaling \$44,718. These deficiencies fell into four categories: no supporting documentation; payroll unrelated to Partnership contracts; net pay discrepancies; and undocumented and unexplained deductions.

- CEAP failed to submit any payroll information for September and October, 2007 in support of their reimbursement request to the Partnership. Despite this, they were reimbursed a total of \$31,356 for these two months. The Partnership requested the detail after the reimbursements, but CEAP never provided it.
- CEAP submitted and was reimbursed for \$1,789 of payroll expense for an employee who was working full-time at a day care center owned by CEAP's executive director. This expenditure was totally unrelated to either of the two contracts between CEAP and the Partnership.
- CEAP submitted net pay information to the Partnership in excess of the amounts actually paid to the employees. We discovered this discrepancy during a comparison of net pay per CEAP payroll journals with the cashed check amounts per the bank statements. The total excess amount reimbursed by the Partnership was \$6,383.
- CEAP submitted payroll information showing employee payroll deductions that were totally unrelated to payroll taxes and which were undocumented and unexplained.

FINDINGS AND RECOMMENDATIONS (CONTINUED)

They received reimbursement from the Partnership for these deductions. These deductions were often substantial, sometimes amounting to 50 percent of gross pay. The total amount of these undocumented and unexplained, non-tax deductions amounted to \$5,190.

These payroll-related losses may have been avoidable if the Partnership had exercised greater diligence with respect to requirements for detailed supporting documentation. The Partnership had the ability to withhold payment to CEAP for failure to provide requested documentation, but elected not to use it.

RECOMMENDATION

All reimbursements for the contractor's payroll costs should be supported by employee time sheets, payroll journals, and supporting documentation for the work performed by each employee.⁶ Proof of payment should be verified through a review of canceled checks and/or bank statements. The Partnership's board of directors should exercise its contractual right to withhold payment from a contractor when supporting documentation is requested, but not provided.

4. CEAP MADE PURCHASES DURING THE FINAL MONTH OF THE CONTRACT THAT WERE UNALLOWABLE UNDER SMART START COST PRINCIPLES.

During the final month of its contracts which had expiration dates of June 30, 2008, CEAP made \$3,168 of purchases which were clearly not reasonable. The contracts between CEAP and the Partnership required that CEAP adhere to Smart Start Cost Principles. Under these principles, a cost is reasonable if, in its nature or amount, it does not exceed that which would be prudent under the circumstances prevailing *at the time the decision is made to incur the cost* (italics added).

- On June 17, 2008, CEAP purchased two bookcases and three desks for \$961 and was reimbursed with Smart Start funds. Only nine working days remained until the contract expiration date.
- On June 20, 2008, CEAP purchased two desktop computers for \$498 each and was reimbursed with Smart Start funds. Only six working days remained until the contract expiration date.
- On June 26, 2008, CEAP purchased 25 fabric stacking chairs for \$907 and was reimbursed with Smart Start funds. The delivery date was scheduled for June 27, which left one day to use them.

⁶ Examples of supporting documentation include contact summary sheets (shows the name of the child care facility visited, employee's arrival time, work performed, employee's departure time, and the signature of the facility's owner or director) and detailed employee mileage logs.

FINDINGS AND RECOMMENDATIONS (CONTINUED)

- On June 26, 2008, CEAP purchased two bookcases and two leather chairs for \$304 and was reimbursed with Smart Start funds. The delivery date was scheduled for July 3, or 3 days after the contracts with the Partnership expired.

The contracts with CEAP were set to expire in a matter of days without any guarantee of renewal. There was no obligation for CEAP to perform any further services after the contracts expired. The expenditures were not for items such as educational materials for day care centers or day care providers, but rather for office furnishings, computers and supplies for the CEAP office. We do not believe that either of the contracted programs received any benefit from these expenditures. In our opinion, each of these expenditures violated Smart Start Cost Principles based on their nature and timing.

RECOMMENDATION

The Partnership should apply the criteria for reasonableness, as set forth in section A-2 of the Smart Start Cost Principles (see Appendix B), to all contractor purchases. The Partnership's board of directors should take a more active role in ensuring that reimbursement requests meet the requirements for reasonableness set forth in the Smart Start Cost Principles.

5. CEAP USED \$5,000 OF SMART START FUNDS TO PAY INAPPROPRIATE BONUSES.

During the final month of its contract with the Partnership, CEAP paid five \$1,000 bonuses to four day care centers or their owners. The memos on the checks were "Early Bird Bonus." This would indicate that each of the bonus recipients applied to the DHHS⁷ Division of Child Development for an early assessment (for a higher star rating). However, none of the recipients receiving the bonuses applied for an early assessment, according to the Division of Child Development. Therefore, even if such an incentive had existed, the recipients would not have qualified.

The budget narrative attached to the Quality Enhancement contract contains the term "Early Bird Grants," but provides no further description. Representatives at The North Carolina Partnership for Children and the Partnership were unable to provide us with a definition for "Early Bird Bonus" other than to speculate that it would be payment for an early assessment of a child care facility that results in a higher star rating. Moreover, there is no part of the contract containing a provision for \$1,000 cash incentive or bonus payments. The only incentive that is specifically provided for in the contract is for one time, \$300 payments to child care programs that obtain a new, 3 star license or those that are moving directly to a 4 or 5 star license from a temporary or 1, 2, or 3 star license.

⁷ North Carolina Department of Health and Human Services.

FINDINGS AND RECOMMENDATIONS (CONCLUDED)

RECOMMENDATION

- Bonus or award payments should be verified to determine that such payments are provided for in the contract.
- Bonus or award payments should be verified to confirm recipient eligibility under the criteria established for the bonus or award.
- The Partnership should review all contractor reimbursement requests to ensure that expenditures are allowable under the terms of the contract.

6. THE FIDELITY BOND OBTAINED BY CEAP WAS INADEQUATE TO COVER THE AMOUNT OF SMART START FUNDS AT RISK.

The partnership awarded two contracts to CEAP totaling \$374,261. Under North Carolina General Statute §143B-168.12(c), a fidelity bond is required for contractors of a local partnership receiving more than \$100,000. The fidelity bond obtained by CEAP was for \$10,000. If a claim had been filed under this policy, the maximum amount recoverable would have been \$10,000 and the payment would have been made to CEAP (the named loss payee).

The purpose of the fidelity bond requirement is to provide protection against loss of funds due to embezzlement activities on the part of officers or employees of the contractor. In this case, assuming that a claim had been filed, the maximum recoverable amount would have been far less than the actual losses sustained. Additionally, it would have then been the Partnership's responsibility to attempt to recover the insurance proceeds from CEAP.

RECOMMENDATION

The North Carolina Partnership for Children should develop guidelines for the amounts of the fidelity bonding required under G.S. §143B-168.12(c) and make it part of its fiscal accountability plan as required under G.S. §143B-168.12(a)(4). The guidelines should ensure that the amount of the bond is commensurate with the amount of state funds at risk. The policy revision should also stipulate that the joint loss payee for the fidelity bond is The North Carolina Partnership for Children or the local partnership, as opposed to the contractor or subcontractor only.

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APPENDIX A
NORTH CAROLINA GENERAL STATUTE 14-100

Article 19.

False Pretenses and Cheats.

§ 14-100. Obtaining property by false pretenses.

(a) If any person shall knowingly and designedly by means of any kind of false pretense whatsoever, whether the false pretense is of a past or subsisting fact or of a future fulfillment or event, obtain or attempt to obtain from any person within this State any money, goods, property, services, chose in action, or other thing of value with intent to cheat or defraud any person of such money, goods, property, services, chose in action or other thing of value, such person shall be guilty of a felony: Provided, that if, on the trial of anyone indicted for such crime, it shall be proved that he obtained the property in such manner as to amount to larceny or embezzlement, the jury shall have submitted to them such other felony proved; and no person tried for such felony shall be liable to be afterwards prosecuted for larceny or embezzlement upon the same facts: Provided, further, that it shall be sufficient in any indictment for obtaining or attempting to obtain any such money, goods, property, services, chose in action, or other thing of value by false pretenses to allege that the party accused did the act with intent to defraud, without alleging an intent to defraud any particular person, and without alleging any ownership of the money, goods, property, services, chose in action or other thing of value; and upon the trial of any such indictment, it shall not be necessary to prove either an intent to defraud any particular person or that the person to whom the false pretense was made was the person defrauded, but it shall be sufficient to allege and prove that the party accused made the false pretense charged with an intent to defraud. If the value of the money, goods, property, services, chose in action, or other thing of value is one hundred thousand dollars (\$100,000) or more, a violation of this section is a Class C felony. If the value of the money, goods, property, services, chose in action, or other thing of value is less than one hundred thousand dollars (\$100,000), a violation of this section is a Class H felony.

(b) Evidence of nonfulfillment of a contract obligation standing alone shall not establish the essential element of intent to defraud.

(c) For purposes of this section, "person" means person, association, consortium, corporation, body politic, partnership, or other group, entity, or organization. (33 Hen. VIII, c. 1, ss. 1, 2; 30 Geo. II, c. 24, s. 1; 1811, c. 814, s. 2, P.R.; R.C., c. 34, s. 67; Code, s. 1025; Rev., s. 3432; C.S., s. 4277; 1975, c. 783; 1979, c. 760, s. 5; 1979, 2nd Sess., c. 1316, s. 47; 1981, c. 63, s. 1; c. 179, s. 14; 1997-443, s. 19.25(1).)

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APPENDIX B
SMART START COST PRINCIPLES – SECTION A-2

A-2. Reasonable costs.

A cost is reasonable if, in its nature or amount, it does not exceed that which would be prudent under the circumstances prevailing at the time the decision is made to incur the cost. In determining the reasonableness of a given cost, consideration shall be given to:

- a. Whether the cost is of a type generally recognized as ordinary and necessary for the operation of the organization or the performance of services.
- b. The restraints or requirements imposed by such factors as generally accepted sound business practices, fair and open competitive bidding, Federal and State laws and regulations, and terms and conditions of the Smart Start contract or grant agreement.
- c. Whether the individuals concerned acted with prudence in the circumstances, considering their responsibilities to the organization, its members, employees, and clients, the public at large, and the State.

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RESPONSE FROM HARNETT COUNTY PARTNERSHIP FOR CHILDREN



PO Box 70 • 1901-G N Main Street • Lillington • NC 27546 • Phone: (910) 893-2344 • Fax: (910) 893-2387 • www.harnettsmartstart.org

May 10, 2010

Ms. Beth A. Wood, CPA, State Auditor
State of North Carolina Office of the State Auditor
2 S. Salisbury Street
20601 Mail Services Center
Raleigh, NC 27699-0601

Dear Ms. Wood:

Thank you for the opportunity to respond to the report on the investigation of allegations concerning Community Education and Programs, Inc. (CEAP), a contractor utilized by the Harnett County Partnership for Children (HCPC). We have carefully reviewed the findings and recommendations made by the Office of the State Auditor. Our responses are respectfully presented below.

Finding 1. CEAP fraudulently obtained Smart Start reimbursements through vendor invoicing.

Recommendation 1. The Partnership should not make cash advances to contractors unless specifically required to do so under the terms of the contract. ... The Partnership should only accept original invoices (no photocopies) as proof of payment.

HCPC Response: HCPC concurs with this recommendation and will not authorize cash advances that do not comply with contract terms. Additionally, monitoring procedures have been strengthened to include verification of original invoicing during on-site monitoring visits. Third party verification will be conducted where amounts are significant and /or documentation appears questionable.

Finding 2. CEAP fraudulently obtained Smart Start reimbursements for payroll taxes.

Recommendation 2. The Partnership should require the contractor to provide documentation which is sufficient to substantiate the amount of payroll tax liability and proof of payment. ... Payroll tax filings (e.g., IRS Form 941) should also be reviewed to determine that reimbursed wages and tax payments equal the amount remitted to tax authorities.

HCPC Response: HCPC concurs with this recommendation and will revise policies to require contractors to submit documentation substantiating the amount of payroll tax liability and proof of payment. Additionally, as noted above, monitoring procedures have been strengthened to include verification of original tax documents during on-site monitoring visits.

Finding 3. CEAP obtained Smart Start reimbursements for payroll expenses that were undocumented or unrelated to their contracts.

Recommendation 3. All reimbursements for the contractor's payroll costs should be supported by employee time sheets, payroll journals, and supporting documentation for the work performed by each employee. ...

HCPC Response: HCPC concurs with this recommendation and will exercise greater diligence with respect to requirements for detailed supporting documentation. Additionally, HCPC will exercise its contractual right to withhold payment from a contractor when sufficient supporting documentation is not provided or in cases of noncompliance.

Finding 4. CEAP made purchases during the final month of their contract that were unallowable under Smart Start Cost Principles.

Recommendation 4. The Partnership should apply the criteria for reasonableness, as set forth in section A-2 of the Smart Start Cost Principles (see Appendix B), to all contractor purchases. ...

HCPC Response: HCPC concurs with this recommendation and will exercise greater diligence in applying the criteria for reasonableness as set forth in the Smart Start Cost Principles to ensure that all reimbursement requests comply with Smart Start Cost Principles. Additionally, HCPC will exercise its contractual right to reduce the amount of the final draw, when warranted.

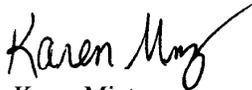
Finding 5. CEAP used Smart Start funds to pay inappropriate bonuses.

Recommendation 5. Bonus or award payments should be verified to determine that such payments are provided for in the contract. Bonus or award payments should be verified to confirm recipient eligibility under the criteria established for the bonus or award. The Partnership should review all contractor reimbursement requests to ensure that expenditures are allowable under the terms of the contract.

HCPC Response: HCPC concurs with this recommendation and has strengthened policies and procedures related to the payment of bonuses/awards to ensure that recipient eligibility is confirmed prior to bonus/award payments and that payments are provided for under the terms of the contract.

We appreciate the professional manner in which this investigation was conducted and would like to express our gratitude to the Office of the State Auditor for its assistance throughout this process. As mentioned in the report, the Partnership experienced turnover in three key positions (Executive Director, Finance Manager and Program Manager) during the fiscal year ended June 30, 2008, and we feel it is relevant to point out that the activities/events outlined in this report occurred during this period of transition, prior to the current administration. We feel confident that the constructive recommendations provided in this report will strengthen operations and improve the quality of services provided by the Harnett County Partnership for Children.

Sincerely,



Karen Mintz
Board Chair

cc: Tommy Burns, HCPC Chair-Elect
Lisa Familo, HCPC Executive Director



May 20, 2010

Ms. Beth A. Wood, CPA
State Auditor
Office of the State Auditor
2 S. Salisbury Street
20601 Mail Service Center
Raleigh, NC 27699-0601

Dear Ms. Wood:

Our response to the investigative audit of Community Education and Programs, Inc. (CEAP) is below.

Recommendation:

The North Carolina Partnership for Children should develop guidelines for the amounts of the fidelity bonding required under G.S. §143B-168.12(c) and make it part of its fiscal accountability plan as required under G.S. §143B-168.12(a)(4). The guidelines should ensure that the amount of the bond is commensurate with the amount of state funds at risk. The policy revision should also stipulate that the joint loss payee for the fidelity bond is The North Carolina Partnership for Children or the local partnership, as opposed to the contractor or subcontractor only.

Response:

The North Carolina Partnership for Children, Inc. (NCPC) concurs with the recommendations. NCPC will revise its Fiscal Accountability Plan to incorporate requirements that address the amounts of fidelity bonding coverage of local partnership subcontractors and the addition of the local partnership on the subcontractor's policy.

We appreciate the professionalism of the auditors and the opportunity to respond to these issues.

Sincerely,

A handwritten signature in black ink that reads "Ashley O. Thrift". The signature is written in a cursive, flowing style.

Ashley O. Thrift
Board Chair

/dm

cc: Stephanie Fanjul, President

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ORDERING INFORMATION

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