STATE OF
NORTH CAROLINA

PERFORMANCE AUDIT

CHILD CARING INSTITUTIONS

JUNE 2006

OFFICE OF THE STATE AUDITOR

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The Honorable Michael F. Easley, Governor
Members of the North Carolina General Assembly
Ms. Carmen Hooker Odom, Secretary
North Carolina Department of Health and Human Services

Ladies and Gentlemen:

We are pleased to submit this performance audit entitled *Child Caring Institutions*. The objectives of this audit were to examine the cost allocation processes of the child caring institutions, evaluate administration rates, review the institutions' utilization rates, examine the rate-setting methodology, and make recommendations on ways to improve the rate-setting process. Secretary Odom has reviewed a draft copy of this report. Her written comments are included after each audit finding.

We wish to express our appreciation to the staff of the Department of Health and Human Services for the courtesy, cooperation, and assistance provided us during the audit.

Respectfully submitted,

Leslie W. Merritt, Jr.

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SUMMARY

Foster care is a temporary living arrangement for abused, neglected, and dependent children who need a safe place to live when their parents or a relative cannot take care of them. Foster care is provided through child caring institutions, family foster homes, therapeutic family foster care or foster/adoptive families. Child caring institutions are defined by the Social Security Act under the Federal Title IV-E Foster Care program as private child care institutions, or a public child care institution which accommodates not more than 25 children, are licensed or approved by the State, but does not include detention facilities, forestry camps, training schools, or facilities operated primarily for the purpose of detention of children who are determined to be delinquent. North Carolina licenses child caring institutions as child placing agencies or child caring agencies. Child placing agencies are private, non-profit, or for profit agencies that place children in residential child caring institutions, family foster homes, therapeutic foster homes or adoptive homes. Child caring agencies operate institutional homes, emergency shelters, group homes, camps, maternity homes, or mental health residential treatment facilities.

The Controller's Office of the Department of Health and Human Services is responsible for the determination of individual institution reimbursement rates based on Federal Title IV-E foster care rate-setting requirements. Child caring institutions interested in participating in the Title IV-E rate-setting process must enter into a formal agreement with the Division of Social Services and submit annual financial information to the Department. Sixty-six child caring institutions participated in rate setting during the fiscal year of 2003-04.

The objectives of this audit were to examine the cost allocation processes of the child caring institutions, evaluate administration rates, review the institutions' utilization rates, examine the rate-setting methodology, and make recommendations on ways to improve the rate-setting process.

RESULTS IN BRIEF

The current rate-setting methodology does not provide the child caring institution with any incentives to contain costs. Most of the institutions participating in the Title IV-E program are provided rates that enable them to have most of their allowable costs reimbursed for their Title IV-E eligible children. This methodology rewards the institution for spending additional dollars and produces a wide range of reimbursement rates among institutions providing similar program services.

The per diem reimbursement rate for the foster care program could decrease significantly if more of the bed-day capacity of the institutions were utilized. The average institution utilization rate was 55%. The utilization rate shows the efficiency level of the foster care program based on the usage of the beds assigned and available for each institution. Higher utilization results in a lower per diem cost.

In August 2004, the Department of Health and Human Services established the Foster Care Rate Structure Group. The goal of the group is to review the rate-setting process for foster care programs and develop standard reimbursement rates based on a newly defined cost

model. The North Carolina General Assembly passed legislation in the summer of 2005 requiring the Department of Health and Human Services to establish standardized rates for child caring institutions throughout the State. These rates should be effective beginning July 1, 2006. The proposed model establishes rates that are significantly less than the current average institutional reimbursement rates.

Oversight over the rate-setting process is lacking and hampered by program complexity, inadequately written procedures and processing delays. The Department has not established sufficient programmatic oversight over the rate setting process. There is very little to no evidence that analytical reviews, cost analysis and comparisons, inquires or any other form of rate management was employed by the Department.

The social workers component in the proposed cost model is unclear. The Department appears to be unsure regarding the need of social workers in residential foster care programs. Costs for social workers were built into the model, but at a lower hourly wage than the average wages for social workers.

The Department's rate-setting calculation resulted in an over allocation of $400,000 in indirect administration costs to the foster care program.

DEPARTMENT'S RESPONSE

The responses from the Department of Health and Human Services are included after each recommendation.

INTRODUCTION

BACKGROUND

The objective of the Foster Care program is to provide safe, appropriate, 24-hour substitute care for children who are under the jurisdiction of the administering State agency and need temporary placement and care outside their home. Foster care assistance funding provides payment for food, shelter, clothing, personal incidentals, school supplies, usual transportation expenses and certain other expenses while the child is in the placement responsibility of a county department of social services. This funding is available regardless of how the child comes into the agency's placement responsibility, whether it was a result of a voluntary placement agreement, non-secure custody order, adjudication of abuse, neglect, dependency, undisciplined, or delinquency, or through relinquishment of parental rights.

The Division of Social Services began establishing individual foster care facility rates in 1992. The implementation of this program established a formal process for foster care cost funding for qualified residential child caring institutions and private child-placing agencies. These institutions provide family foster care, therapeutic foster care, group, institutional, emergency and therapeutic camps services. Child caring institutions wishing to participate in the Title IV-E program and receive reimbursements from the State must qualify through the Division of Social Services by entering into a formal agreement. To apply for an individual institution rate, these institutions must have been in operation for at least one year and must submit information to the Department of Health and Human Services Controller's Office for determination of the individual rates based on the Title IV-E foster care rate-setting requirements.

The rate setting branch of the Controller's Office of the Department of Health and Human Services receives the reports from the applicant agencies, reviews all information, and determines the individual rates. The rate setting branch facilitates a meeting with the policy committee of the North Carolina Children & Family Services Association[1] to review the lists of proposed rates and recommend a cap (maximum/ceiling rate) for each type of care as required by the North Carolina Administrative Code. The rate setting branch then meets with the Division of Social Services to present the recommended cap for approval. The final step is approval of the individual institution rate by the Rate Setting Review Board chaired by the Secretary of the Department of Health and Human Services. A notification letter is sent to each institution confirming its rate.

OBJECTIVES, SCOPE, AND METHODOLOGY

The scope of this audit was established in the General Assembly's 2005 Session Laws 2005-276, Section 10.47.(a). This legislation required the Office of the State Auditor to conduct an audit to evaluate overhead rates and reimbursements for child caring institutions

[1] The Association is composed of North Carolina not-for-profit, for-profit, and public providers of services to children and families.

receiving state funding. Our discussion of the requirements specified by the legislation is organized around two audit objectives:

A. *What is the current rate-setting methodology?* We will provide information on the cost allocation processes used by child caring institutions, the methodology used to assign direct and indirect costs, and whether the allocated costs are consistent among the various child caring institutions. We will compare the administrative costs charged by North Carolina child caring institutions with other similar type non-profits and we will discuss the impact utilization has had on rates.

B. *Recommendations on how to develop and maintain equitable rates.* Rate-setting methodologies used by other states will be presented as well as how North Carolina's payments to child caring institutions compare to other states. We will offer recommendations on the proposed rate setting process.

To accomplish the audit objectives, we reviewed the Department's rate-setting process for foster care reimbursements, concentrating on the 66 child caring institutions that submitted cost reports for the 2005-06 individual institution rates. We examined and analyzed the child caring institutions' cost reports, interviewed Department of Health and Human Services personnel, visited and/or contacted multiple child caring institutions, and examined the rate-setting methodologies from other states. We reviewed the Federal regulations, the North Carolina General Statutes and the Administrative Codes relating to the foster care program and the Department's policies and procedures. We also reviewed internal controls, examined financial records and documentation as they related to the Department's rate-setting activities.

This report contains the results of the audit including conclusions and recommendations. Specific recommendations related to our audit objectives are reported. Because of the test nature and other inherent limitations of an audit, together with the limitations of any system of internal and management controls, this audit would not necessarily disclose all weaknesses in the systems or lack of compliance.

We conducted the fieldwork from November 2005 to March 2006. We conducted this audit under the authority vested in the State Auditor of North Carolina by Section 147-64.6 of North Carolina General Statutes and according to generally accepted government auditing standards.

A. THE CURRENT RATE-SETTING METHODOLOGY

OVERVIEW OF RATE-SETTING PROCESS

The purpose of the rate-setting process utilized by the Department of Health and Human Services is to provide each of the 66 child caring institutions with a rate for each foster care program it operates. Rates are established for an institution licensed as a child placing agency and/or child caring institution. Child placing agencies are private, non-profit, for profit or governmental facilities that have responsibility for placing and monitoring children in residential child caring institutions, family foster homes, therapeutic family foster homes or adoptive families. Child caring institutions provide direct care services to children and can be comprised of institutional homes of 10 or more children, emergency shelters, group homes, therapeutic camps, or mental health residential treatment facilities providing high-risk intervention.[2]

Institutions that participate in the Title IV-E program must enter into a formal agreement with the Division of Social Services of the Department of Health and Human Services. In order to receive an individual facility rate, it must have been in operation for 12 months and must submit various documents and certifications. Included among the information required is documentation of the number of child care days provided, a completed Residential Treatment and Foster Care Report (cost report), and the institution's most recent independently audited financial statements. The audited financial statements must show both revenues and expenditures and must separate administration costs from program costs. Direct program, fund-raising, and indirect administration costs are separately reported in the financial statements audited by independent auditors. The institution and its independent auditor must also attest to the break out of expenditures stated in the cost report. Expenses reported on the cost report must agree with the institution's audited financial statements.

The rate setting branch of the Department of Health and Human Services' Controller's Office reviews each institution's materials for completeness and accuracy and determines the institution's Title IV-E rate using a predefined formula.

The North Carolina Administrative Procedure Act requires that institution rates be shared with the Children and Family Services Association of North Carolina. The Association is required to review the rates and recommend a cap or ceiling for each type of care. The Division of Social Services reviews the recommended caps and then either accepts the recommended caps or establishes its own. Following Division of Social Services approval, the Rate Setting Review Board under the Secretary's Office of the Department of Health and Human Services considers the recommended caps and the individual institution rates for approval. Once all approvals are in place, any institution with a rate exceeding the cap rate is assigned the cap rate. Institutions below the cap rate receive the rate established for that institution by the Department.

[2] Use of "child caring institution" or "institution" in this report should be understood as referring to both child placing agencies and child caring institutions.

COST REPORT

The cost report establishes a standard method of reporting costs by child caring institutions. It provides historical data on the cost of providing child care services. It accumulates and categorizes a child caring institution's costs of running its programs and activities. An institution's rate is based on the expenses it incurred two years before the year for which the rate is applicable. The rate is adjusted for two years of inflation to arrive at a rate for the current year. The information presented in the tables and charts throughout this report is a summation of those child caring institutions' data categorized as family foster care, institutional group care, group home care, emergency home care and therapeutic camping. Unique characteristics or statistics of individual child caring institutions are not presented or discussed. Our analysis was based on the information contained in the Department's 2003-04 cost reports database.

Cost Report Data Reported By Child Caring Institutions
For the rate setting year ended June 30, 2006

	Foster Family Care	Institutional Group Care	Group Home Care	Emergency Home Care	Therapeutic Camping	Other Activities/ Programs	Total Reported on Cost Reports
Program Costs:							
Treatment Expenses	$ 0	$ 0	$ 0	$ 0	$ 0	$ 20,351,182	$ 20,351,182
Program Salaries	938,659	16,145,499	8,343,030	4,305,503	7,692,417	13,476,372	50,901,480
Social Worker Salaries	5,746,851	2,701,732	1,415,372	1,284,565	1,545,481	3,804,069	16,498,070
Foster Care Board Payments	12,826,646	5,955,307	1,738,205	894,632	2,704,699	17,134,917	41,254,406
Depreciation	195,628	2,068,925	533,363	193,527	801,611	2,474,008	6,267,062
'Total Program Costs	19,707,784	26,871,463	12,029,970	6,678,227	12,744,208	57,240,548	135,272,200
Administration Costs:							
Administrative Costs (Allocated by CCIs)	4,028,890	3,558,948	1,865,876	937,857	1,321,134	54,905,796	66,618,501
Administrative Costs (Allocated by DHHS)	3,196,756	4,238,948	1,869,217	1,025,212	2,113,849	18,510,367	30,954,349
Total Administration Costs	7,225,646	7,797,896	3,735,093	1,963,069	3,434,983	73,416,163	97,572,850
Total Allowable Costs	26,933,430	34,669,359	15,765,063	8,641,296	16,179,191	130,656,711	232,845,050
Non-Allowable Costs Reported	227,816	1,311,662	157,647	43,964	1,820,913	28,319,890	31,881,892
Total Amounts Reported by CCIs	$ 27,161,246	$ 35,981,021	$ $15,922,710	$ 8,685,260	$ 18,000,104	$ 158,976,601	$ 264,726,942
Administration as a % of total allowable costs	27%	22%	24%	23%	21%		

Facility Rates Computed From Above Data and Allowed to Child Caring Institutions
In effect for year ended June 30, 2006

	Foster Family Care	Institutional Group Care	Group Home Care	Emergency Home Care	Therapeutic Camping
Facility Rates (per child per month):					
Maximum	$ 3,662	$ 6,263	$ 6,097	$ 6,162	$ 3,980
Minimum	995	3,411	2,307	2,918	3,415

The cost report includes both foster care expenses and other program expenses. The costs are categorized by Foster Care programs, the Medicaid program, other programs, fund raising, and administration. Some institutions participate in only foster care programs, some have both foster care and Medicaid treatment programs, and others also have broaden their services to include schools, counseling, mentoring, day care programs. While the majority of institutions performed their accounting functions in-house, many contracted with independent accounting firms to provide financial services and reports. Software accounting systems varied among the institutions and the accounting firms.

Costs are reported on the cost reports by programs/activities in three general categories: program costs, administration costs, and non-allowable costs. A category may contain several major sub groupings of costs, which are defined in more detail in the appendix to this report.

Program costs are those costs associated with the children's immediate needs. They include salaries and wages, benefits and payroll taxes of direct care workers and social workers and their supervisors. They also include cost of housekeeping, shelter, personal needs, clothing, limited recreation costs, school supplies, and transportation. These costs are incurred either directly by a particular program or are allocated by the institution. If allocated, they are based on bed days, square footage, staffing levels, percentage of time spent in each program, or a combination thereof.

Administration costs include both direct and indirect administrative costs. Direct administrative costs are those costs specifically identifiable with the administration of a particular program or activity. These costs include such items as office expense, insurance, professional fees, taxes, interest, seminars and conferences, and administrative salaries.

Indirect administrative costs are those administrative costs that have been incurred for common or joint purposes. These costs benefit more than one program or activity. They are allocated to an institution's programs/activities as a percentage of that program's allowable cost to total costs reported.

Non-allowable costs are those costs that are not reimbursable according to a particular program's guidelines. As for Title IV-E programs, non-allowable costs include day care, social services, higher education, bad debts, in-kind contributions, penalties, extraordinary items, and other miscellaneous costs.

Foster care program costs were charged in several different ways, depending largely on the number of programs the institution operated, as shown on the following table:

Method of Charging Costs	Number of Institutions	Percent
Institutions that recorded costs in only one program; therefore, no allocation of expenses was required	33	50
Institutions that have multiple foster care programs and charged directly associated costs to each program	4	6
Institutions that allocated costs based on bed day usage	15	23
Institutions that used a combination of charging directly associated costs to a program and allocating some costs among programs using multiple methods such as bed days, square footage, time spent on programs, staffing levels and percent of program expenses to total expenses	10	15
Institutions that allocated costs based on multiple methods such as bed days, square footage, time spent on programs, percent of program expenses to total expenses and staffing levels	4	6
Totals	66	100

ADMINISTRATION COSTS

We examined the individual institution's foster care administration costs and compared those with the total overall average administration costs for all institutions operating foster care programs in North Carolina. The total administration costs for all foster care programs averaged 26% of total expenses.

Administration % Range	Number of Institutions
1% - 10%	4
11% - 20%	20
21% - 25%	15
Average 26%	2
27% - 30%	8
31% - 40%	13
41% - 64%	3
65%	1

IMPACT THAT UTILIZATION HAS ON RATES

The utilization rates are based on the actual number of beds utilized compared to the maximum number of beds assigned/licensed to an institution. The utilization rate shows the efficiency level of the foster care program based on the usage of the beds assigned and available for each institution. Each institution has a maximum number of licensed beds assigned for each program. The number of beds used provides the institution with its occupancy rate, i.e. its utilization rate. The majority of the institutions served both Medicaid eligible and Title IV-E eligible foster children. Child care days for each program are recorded separately.

As the institution's utilization rate increases, certain variable operating costs (food, utilities, personal care, etc.) should also increase while the fixed operating costs (rent, mortgage, depreciation) should remain reasonably constant depending on the licensed capacity of the institution. As utilization increases, the cost per child day to provide services to the children should decrease.

We computed the utilization rates based on the data from the 2003-04 cost reports. The average institution utilization rate, including Medicaid treatment bed days and foster care bed days, was 55%. This rate was based on the total number of actual bed days reported compared to total licensed bed days. The utilization rates for individual institutions ranged from 16% to 100%.

Another analysis compared only foster care bed days to the total licensed bed days. The utilization rate was 42% for all foster care programs. The utilization rates for individual institutions ranged from 1% to 100%. Individual program rates under foster care were: family foster care @ 31%, institutional group care @ 52%, group home care @ 54%, emergency care @ 67%, and therapeutic camp care @ 88%.

Foster Care Rate Reduction Based on 80% Utilization

	Average Capped Facility Rate	Percentage Saving @ 80% Utilization	Dollars Savings	Reduced Facility Rate
Foster Family Care	$ 2,098	16%	$ 336	$1,762
Institutional Care	4,883	34%	1,660	3,223
Group Care	4,979	23%	1,145	3,834
Emergency Care	5,103	13%	663	4,439
Therapeutic Camp	3,698	N/A, program currently above 80%		

Higher utilization results in a lower per diem calculation and, inversely, lower utilization results in a higher per diem calculation. Assuming the individual programs could attain a utilization rate of 80%, the per diem rate for each foster care program would decrease as noted in the table.

B. RECOMMENDATIONS ON HOW TO DEVELOP AND MAINTAIN EQUITABLE RATES

1. THE DEPARTMENT SHOULD BRING TO FRUITION ITS EFFORTS TO DEVELOP A STANDARD RATE FOR INSTITUTIONS IN THE FOSTER CARE PROGRAM

The current rate-setting methodology for the foster care program does not provide the child caring institution with any incentives to contain costs. Excluding those institutions above the rate cap, typically about 65% of the institutions participating in the Title IV-E program are provided rates that enable them to have most of their allowable costs reimbursed for their Title IV-E eligible children. There are no requirements or policies and nothing in the contracts with the institutions that requires or even encourages the institutions to contain costs. The more an institution spends, the higher its reimbursement rate from Title IV-E funding. This methodology rewards the institution for spending additional dollars and produces a wide range of reimbursement rates among institutions providing similar program services.

North Carolina 2006 Monthly Reimbursement Rates Per Child

	Minimum Rate	Maximum Rate
Foster Family Care	$ 995	$3,662
Institutional Group Care	3,411	6,263
Group Home Care	2,307	6,097
Emergency Home Care	2,918	6,162
Therapeutic Camping	3,415	3,980

Our survey of other states' efforts to institute competition for foster care services yielded little to no directly applicable information. However, other states have developed standard reimbursement rates based on levels of care, three of which we will discuss.

- Georgia has monthly rates for standard room and board similar to North Carolina. These rates are set as needed by the Georgia State Legislature. Georgia has established six levels of care for child caring institutions and child placing agencies. Each level of care has standardized per diem rates.

Monthly Reimbursement Rates of Sister States Per Child

	Georgia	South Carolina	Tennessee
Foster Family Care	$1,034 - 5,992	N/A	$1,481
Institutional Group Care	N/A	$2,072 - 4,229	3,296
Group Home Care	2,190 - 9,763	4,106	2,651
Emergency Home Care	N/A	1,064 - 5,170	1,530
Therapeutic Camping	N/A	3,193	3,296

- South Carolina has monthly rates for standard room and board based on the age of the child. The South Carolina Legislature sets standardized rates every five years. South Carolina has three levels of care and per diem rates for therapeutic foster care, family foster care, group foster home, maternity, and emergency shelter services. Cost reports from private specialized group home and residential treatment facilities are used to establish the per diem rates.

- Tennessee has monthly rates for standard room and board according to the age of the child. Tennessee also has standardized reimbursement rates for different levels of care provided. Tennessee has four basic rates for foster homes that are directly contracted, four extraordinary rates, and 14 levels of care which are also contracted with residential providers. Rates are set once every three years by the Tennessee Legislature, with rates being adjusted for inflation and other factors during the years between cost reports.

We also compared North Carolina foster care room and board payments with room and board payments made by some of our sister states. Foster care room and board payments are the basic living expenses of a child in a residential setting including room, board, incidentals and normal daily supervision.

State Room and Board Rates Compared To Sister States

As of April 12, 2006

Children Ages	North Carolina	Other States Average	Percent Difference
0-5	$ 390	$ 411	-5%
6-12	440	438	0%
13-18	490	508	-4%

Other states: Georgia, South Carolina, Tennessee

In August 2004, the Department of Health and Human Services established the Foster Care Rate Structure Group in response to requests made by members of the Children and Family Services Association of North Carolina. The goal of the group is to review the rate-setting process for foster care programs and develop standard reimbursement rates based on a newly defined cost model for all children regardless of eligibility. The North Carolina General Assembly passed legislation in the summer of 2005 requiring the Department of Health and Human Services to establish standardized rates for child caring institutions throughout the State. These rates should be effective beginning July 1, 2006.

The proposed model envisions three rates depending on the level of care (children under 6, children ages 6-12 and children ages 13 and older). The rates are the same regardless of whether the care is related to institutional group, group home, emergency, or therapeutic camp care. In the proposed model, these four types of care have been consolidated under a single “residential care program” rate. The proposed model also changes the family foster care program by incorporating the same age ranges as the residential care program. The Foster Care Rate Structure Group has not released its final report of the new cost model and reimbursement rates, but as of May 23, 2006, we have been provided information regarding the rates that are likely to be proposed. The table that follows displays the Department’s proposed rates as compared with the existing reimbursement rates. Since the current system establishes a rate for each individual institution, the existing reimbursement rates presented in the table represent the average of all institutions for a particular category of care.

Modeled Versus Existing[1] Monthly Rates

	Family Foster Care			Institutional			Group			Emergency			Therapeutic Camp		
Children Ages	Proposed	Existing		Proposed[2]	Existing		Proposed[2]	Existing		Proposed[2]	Existing		Proposed[2]	Existing	
0-5	$1,467	$2,145	-32%	$5,327	$4,987	7%	$5,327	$5,085	5%	$5,327	$5,211	2%	$5,327	$3,776	41%
6-12	1,538	2,145	-28%	3,462	4,982	-31%	3,462	5,080	-32%	3,462	5,206	-34%	3,462	3,773	-8%
13-18	1,608	2,145	-25%	3,553	4,982	-29%	3,553	5,080	-30%	3,553	5,206	-32%	3,553	3,773	-6%

[1] Existing rates for 2005-2006 increased by inflation rate to bring to 2006-2007 equivalence

[2] Proposed residential rate does not differentiate among these Title IV-E program categories

The model recommends a 1 to 5 direct care staff to child ratio. For children 6 years and older, the model suggests a 1 to 10 direct care staff to child ratio. In addition, the model establishes a supervisory staff to direct care staff ratio of 1 to 15. These staffing ratios are the current minimum staffing requirements for licensure in North Carolina. Staff wages and benefits for these direct care workers are based on the median hourly wage statistics for North Carolina for May 2004, taken from the US Department of Labor, Bureau of Labor Statistics. In addition to direct care staff, the model includes a cost component for social workers and social worker supervisors.

The capital costs component of the rate is still under development. The proposal is based on a concept of a fair market rental value of the institution's capital costs that reflects current property values of the county in which the institution resides. This will be similar to the capital cost component reimbursement concept utilized in the Adult Care Home program. The administration component of the modeled rate is also under development. Costs are expected to be based on the average percentage of total direct and indirect administration cost to total program costs.

Recommendation: A standardized rate structure has support from the foster care community in North Carolina and the rationale has gained a base in other states. The Department of Health and Human Services should continue its project to revise the current rate-setting methodology and to develop a standard rate for all institutions in the foster care program. The Department should construct a rate structure that encourages institutions to provide the best services at the lowest possible cost.

Agency's Response: As the audit report indicates, DHHS in August 2004 established the Foster Care Rate Structure Group with the goal of implementing a standardized rate structure based on best practices, which is fair and encourages efficiencies in both costs and the provision of services. The broad-based committee has completed the assigned task and should finalize the draft report within the next thirty days (in June 2006).

2. BETTER MONITORING AND WRITTEN PROCEDURES ARE NEEDED TO ELIMINATE MISTAKES AND ENSURE FAIR STANDARDIZED RATES

Oversight over the rate-setting process is lacking and hampered by program complexity, inadequately written procedures and processing delays. Because of a lack of sufficient and clear instructions regarding cost report preparation, there is little assurance that the cost report data submitted by the institutions has been correctly reported. As a result, the Department cannot be assured that the rates produced by the current process have been properly prepared nor can the Department be assured that the proposed standardized rate-setting process will produce correct rates.

The Department has not established sufficient programmatic oversight over the rate setting process. Although there was evidence of the Department's efforts to ensure the accuracy of data inputs into the cost reporting process, we saw very little to no evidence that analytical reviews, cost analysis and comparisons, inquires or any other form of rate management was employed by the Department. Cost allocation methodologies are not validated because relevant data is not requested from institutions. Inquiries about the composition of miscellaneous charges are not made. Supporting details concerning the nature of contracted management services are not obtained. The staffing levels (full-time equivalents) are not separately requested for social workers, managers, direct care workers, supervisors, and administrative workers and charges to these as well as other cost categories are not monitored and assessed. The Department does not compare cost elements between years or among institutions to consider trends or to evaluate data integrity. Utilization rates and direct program and administrative costs are not evaluated. No periodic on-site monitoring of institutions is performed.

Also, the Department's process could be aided by better-written instructions. The Title IV-E cost process is complex due to rules governing the program, to changes of interpretation of these rules, and to other situations such as remote corporate administration and the use of subcontracting services. In this environment, there is a need for clear instructions regarding the entire rate setting process. The Department's written instructions do not sufficiently explain how to complete the cost reports. The instructions on the importance of accurately allocating common costs among programs are not sufficient for key cost items.

Multiple revisions of cost reports were requested from institutions due to errors identified by the Department. Several institutions submitted cost reports too late to be considered in the rate setting review process. In many cases, only the summary and not the detailed line items were available for review by the Department.

Recommendation: The Department's new cost model process to establish foster care rates will require detailed analysis of the cost report data. Because the proposed model calls for standardized rates to be re-established every three years, the need to monitor and manage rates will continue. The Department should improve management oversight over foster care program costs and improve policy inputs by monitoring major cost elements, determining and assessing utilization rates and analyzing cost comparisons. The

Department should monitor and perform analytical reviews annually of all cost reports and bed day utilization data. Periodic on-site monitoring to address such areas as staffing levels, administrative procedures, cost allocation methodologies, unallowable costs, and utilization rates should be considered. The Department should provide more detail written instructions for each line item on the cost report. Staff training should be provided.

Agency Response: Detailed procedures and required training are inherent in the current rate setting process. However, due to the nature of the process in the past, the Department staff have not been in the position to perform the steps outlined in the recommendation above. The basic goal in the Rate Setting Branch was to process agency rate requests/cost reports as efficiently as possible in a very short timeframe in order to calculate individual facility rates and set caps on the rates.

However, with the implementation of the standardized rate structure, more time will be available for analysis and the monitoring of costs and allocation methods. During the study, the Foster Care Rate Setting Work Group determined that detailed instructions and in-depth training to providers on definitions and use of the cost reports would be essential to the success of the model. These detailed instructions and training will be provided by the DHHS Controller's Office. The Division of Social Services is responsible for monitoring staffing levels and has recently added additional staff in order to increase the level of compliance oversight.

3. THE STATUS OF THE SOCIAL WORKERS COMPONENT IN THE PROPOSED COST MODEL IS UNCLEAR AND SHOULD BE RECONSIDERED

The posture taken in the proposed cost model on the social workers component in residential foster care programs is unclear and possibly unrealistic. As a result, the model may not have given adequate recognition to all legitimate costs of the program. The model, on the one hand, states "social workers are not specifically required," but "their presence is encouraged." On the other hand, the model specifies a ratio of one social worker to 15 children. Costs for social workers were then built into the model, but at a lower hourly wage than the average wages for social workers.

The wage rate used in the model is $9.35 per hour. This is 43% less than the $16.33 median hourly wage rate for social workers in North Carolina as reported by the U.S. Department of Labor Bureau of Labor Statistics. Department officials have stated the lower hourly rate is used because not all institutions may need to employ social workers. However, data presented to us suggest a large percentage, up to 74%, of the child caring institutions had social workers in residential foster care programs in 2004.

Recommendation: The Department should determine whether there is a need for a social workers component in the model. If the need exists, the Department should consider recognizing the full cost of this component in the model.

Agency's Response: The Department concurs with this recommendation and has determined that a licensed social worker should be a component of the standard rate. Accordingly, the Department will adjust the social worker component of the best practices modeled rate up to the $16.33 median hourly wage rate for social workers in North Carolina. The Division of Social Services will move forward with the rule-making process through the Social Services Commission that requires social workers and social work supervisors in residential child care.

4. THE DEPARTMENT'S RATE-SETTING CALCULATION RESULTED IN AN OVER ALLOCATION OF INDIRECT ADMINISTRATION COSTS TO THE FOSTER CARE PROGRAMS

The rate-setting methodology the Department used to determine rates for the 2006 fiscal year did not allocate administrative costs to the institutions' fundraising activities, resulting in an over-allocation of approximately $400,000 in costs to foster care programs. This method is contrary to the direction in Office of Management and Budget Circular A-122, Cost Principles for Non-Profit Organizations. It states that fundraising and investment activities shall be allocated an appropriate share of indirect administration costs.

Recommendation: The Department should change the indirect administration allocation method to ensure that the appropriate amount of indirect administration cost is distributed to the foster care program.

Agency Response: The practice of excluding fundraising from the allocation of indirect administrative costs had been questioned by the DHHS Controller's Office but there was never a definitive answer as to why this step in the rate setting process was so deliberately instituted. The DHHS concurs with this recommendation and, in future years, this step will be omitted when calculating rates for reimbursement or comparative/analytical purposes.

GLOSSARY

Administrative costs allocated by child caring institutions: Certain administrative costs are allocated by child caring institutions. These costs are administrative costs associated with a particular foster care program. These costs are recorded by the child caring institution on the Department of Health and Human Services residential treatment and foster care cost report. They are either incurred directly by a particular program or are allocated by the institution. If they are allocated, it is based on child care days or another method. These costs include office supplies, vehicle insurance, property insurance, general insurance, automobile and truck maintenance, telephone, postage, dues and subscriptions, legal and accounting, interest on automobiles, mortgage, fixed assets and other purchases, audit, automotive, equipment and office rental, real estate taxes, data processing, travel and entertainment, licensing fees for individuals and facilities, blood-borne pathogen tests and criminal record check fees for non-Medicaid personnel, contracted management services, advertising, printing, meetings, seminars and conferences, miscellaneous expenses and administrative, operational, and maintenance salaries.

Administrative costs allocated by the Department of Health and Human Service: Administration costs that are not directly allocated or assigned to program costs in the institution's financial statements must be reported separately on the cost report. These indirect administration costs are then prorated to each program based on the percentage of individual program costs to the institution's total operating costs. Once the administration costs are allocated, the Department computes the individual institution reimbursement rate. The Department stipulates the methodology for allocating indirect administration expenses to programs based on the individual program cost as a percent of the institution's total operating costs. This methodology is reflected in the Individual Facility Rate Request Form.

Building repairs and maintenance costs are costs of materials and labor to repair and maintain buildings and grounds.

Capital costs – real property are the selected capital cost items used to compute a fair rental value for real property values. Cost items include depreciation, mortgage interest, building repairs and maintenance, and rent.

Depreciation costs are the annual expense write-off of capital expenditures. Costs that add to the permanent value of property or appreciably prolong its intended life are treated as capital costs. These costs are amortized over the asset's life to determine the annual cost that is recorded on the cost report.

Direct administrative costs are those costs associated with the administration of a particular foster care program. These costs are recorded by the child caring institution on the Department's residential treatment and foster care cost report. These costs include office supplies, vehicle insurance, property insurance, general insurance, automobile and truck maintenance, telephone, postage, dues and subscriptions, legal and accounting, interest on automobiles, mortgage, fixed assets and other purchases, audit, automotive, equipment and office rental, real estate taxes, data processing, travel and entertainment, licensing fees for individuals and facilities, blood-borne pathogen tests and criminal record check fees for non-Medicaid personnel, contracted management services, advertising, printing, meetings, seminars and conferences, miscellaneous expenses and administrative, operational, and maintenance salaries.

Emergency home care is provided in a residential setting with nine or fewer children served in crisis usually less than a 90-day stay.

Fair market rental value is defined as a fair return on the property's assessed value.

Fixed costs are those costs that do not normally change with a change in the volume of production units. The production unit for foster care is the child resident day. Fixed costs include general insurance, depreciation and interest on buildings, audit, legal and accounting, building rent and real estate taxes.

Foster care board payments are program-related costs associated with children's room and board. They include the cost of housekeeping, shelter, personal needs, clothing, limited recreation, school supplies, transportation and payments to foster parents. Foster care board payments to foster care parents relate only to the foster family care program.

Foster family care involves foster parents who are recruited, trained and licensed to provide care for children in their homes. Foster parents receive compensation for the child's room, board and other living expenses.

Fundraising costs are those costs related to the mission of raising funds for the institution.

Group home care is provided in residential housing with nine or fewer children with stays that usually exceed 90 days.

Indirect administrative costs are those indirect costs that have been incurred for common or joint purposes. These costs benefit more than one program.

Institutional group care is provided in a residential setting with 10 of more children housed in two or more buildings (campus setting).

Mortgage interest costs are interest costs paid on buildings and building improvements and land and land improvements.

Non-allowable costs are those costs that are not reimbursable according to a particular program's guidelines. As for Title IV-E programs, non-allowable costs include day care, non-residential social services, higher education, bad debts, in-kind contributions, penalties, extraordinary items, and other miscellaneous costs.

Other program costs are those program costs unrelated to foster care or Medicaid. Some examples of other programs are schools, daycare, big brother/big sister, family preservation and substance abuse programs.

Program costs are those costs associated with the children's immediate needs. They include salaries and wages, benefits and payroll taxes of direct care workers and social workers and their supervisors. They also include cost of housekeeping, shelter, personal needs, clothing, limited recreation, school supplies, and transportation.

Program salaries are program-related costs associated with child care workers who tend to children's immediate needs. Included are salaries and wages, benefits and payroll taxes.

Rent is the cost of renting or leasing facilities.

Social worker salaries are program-related costs associated with social workers that help children deal with a variety of mental health and daily living problems to improve overall functioning. Social workers are defined as staff who perform social services activities including, but not limited to foster care intake and case management, foster care training, parent recruitment and training, and home study preparation and supervision. It includes salaries and wages, benefits and payroll taxes.

Therapeutic camping is provided to 40 or fewer children. It offers an overnight camp experience. Camps require applications and have planned admissions.

Treatment expenses are program-related, are allowable by the Medicaid program and are associated with the health care of those Medicaid-eligible children. They include salaries and wages, benefits, payroll taxes, supplies, contract labor, blood-borne pathogen tests, employee criminal record checks and other expenses.

Variable costs are those costs that change with a change in the volume of production units. The production unit for foster care is the child resident day. Variable costs include employee-related expenses such as salaries and wages, room and board related expenses, office supplies, automotive- and equipment-related expenses such as depreciation, insurance, rent, and maintenance; telephone, postage, dues and subscriptions, operating and fixed asset interest, data processing, travel and entertainment, licenses for individuals and the facilities, management services, advertising, printing, meetings, seminars, training and miscellaneous costs.

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