SUBJECT: Audit Report 2008-08 - Child Care Fee Subsidies (CM08029) (City Wide)

RECOMMENDATION:

(a) That report CM08029 respecting Audit Report 2008-08, Child Care Fee Subsidies, be received; and

(b) That the management action plans as detailed in Appendix “A” of Report CM08029 be approved and the General Manager of Community Services direct the appropriate staff to have the plans implemented.

Ann Pekaruk
Director, Audit Services
City Manager's Office

EXECUTIVE SUMMARY:

The 2008 Internal Audit work plan approved by Council included an audit of child care fee subsidies. This review included the management controls in place to ensure child care fee subsidies available to eligible families are being administered effectively and efficiently. Contracts with and payments to third party services providers were also included in the scope of the audit.

The results of the audit are presented in a formal audit containing observations, recommendations and management responses attached as Appendix “A” of Report CM08029.
BACKGROUND:

Under the Day Nurseries Act, the City of Hamilton is the designated Consolidated Municipal Service Manager (CMSM) for the local child care system (including fee subsidies). The Social Development and Early Childhood Services Division of the Community Services Department is responsible for a broad range of services related to the child care fee subsidy program among them including: entering into and managing service agreements with independent child care providers; assessing and monitoring ongoing eligibility for subsidized child care; and managing a waiting list for subsidized child care.

As at June 30, 2008, there were 4,083 children active in the divisional caseload (an increase from 3,613 as at December 31, 2007). Records indicate approximately $11.4 million has been spent as at June 30, 2008 (December 31, 2007 - $15.6 million).

The audit fieldwork was completed in August, 2008. The results of this audit are attached as Appendix “A” of Report CM08029.

The Audit and Administration Committee receives and approves final audit and review reports as part of its responsibilities for the oversight of governance and control.

ANALYSIS/RATIONALE:

The audit reviewed processes related to the establishment of purchase of service agreements with third parties and the processing of monthly payments to these contracted providers. Such payments are based on a combination of: a pre-determined per diem rate based on each provider’s operating budget (City determined); child attendance at the day care centre (Centre provided and City staff reviewed); level of parental contribution (City calculated); and user fees (charged by the City).

The review also assessed processes used to pre-screen applicants, to provide on-going assessment of eligibility and to place children in the child care system. Included in this aspect of the audit was the transition away from a “needs based” fee subsidy determination to an “income based” fee subsidy taking into account a progressive contribution methodology of up to 30% of a family’s adjusted income.

The Division completed a business process review in March, 2008 and is presently engaged in the design and implementation phase, expected to be completed by Quarter 1, 2009. Several of the management action plans in response to the recommendations made indicate integrating recommendations with the new processes forthcoming from the business process review.

The audit resulted in the identification of areas for improvement in relation to financial, operational and administrative controls. A formal audit report containing observations, recommendations and management action plans as well as an Addendum with five (5) items were issued and are attached as Appendix “A” of Report CM08029.
The main recommendations in the report deal with:

- A formula for calculating per diem rates that incorporates a consistent weighting mechanism for cost of care of specific age groups. An independent review of this calculation is also recommended.
- The enforcement of the submission of required documents as per the service agreements with child care providers in order to ensure financial stability and appropriate current insurance coverage.
- Assessment thresholds for assessing service contract applications, an independent review of such assessments and adequate communication for unsuccessful applicants. This would add an extra level of transparency and consistency in the assessment process.
- More effective co-ordination of overpayment recovery practices and results.
- Compliance with Section 66.7 of the Day Care Nurseries Act (“grandparenting provisions”) in which increases in a family’s adjusted income beyond 20% in a year require the application of the income testing methodology for parent contributions rather than the protection of the rate set under the “needs” test.

Addendum items included administrative enhancements such as regular per diem rate reviews (for service providers), wait list removal procedures and a more efficient filing system for clients’ records.

Management and staff have agreed to take actions to implement all the recommendations. Specific action plans can be found in the attached report. Several of the management action plans indicate various completion dates throughout 2009 as business processes are designed and implemented as a result of the Division’s business process review.

ALTENRATIVES FOR CONSIDERATION:

Not applicable.

FINANCIAL/STAFFING/LEGAL IMPLICATIONS:

Financial/Staffing
As management action plans are incorporated into the design and implementation phase of the business process review, there may be some financial and/or staffing issues. They cannot currently be determined. However, the Division has indicated that as this phase of the business process review is completed (approximately Quarter 1, 2009), a report will be presented to the Emergency and Community Services Committee outlining any implications.

Legal
None.
POLICIES AFFECTING PROPOSAL:

Day Nurseries Act

RELEVANT CONSULTATION:

The attached report includes management action plans which reflect the responses of management and staff responsible for the child care fee subsidy program (Social Development and Early Childhood Services, a division of the Community Services Department).

CITY STRATEGIC COMMITMENT:

By evaluating the “Triple Bottom Line”, (community, environment, economic implications) we can make choices that create value across all three bottom lines, moving us closer to our vision for a sustainable community, and Provincial interests.

Community Well-Being is enhanced. ☑ Yes ☐ No

City Council’s vision of “The Best Place to Raise a Child” and its goal of “A Great City in Which to Live” is addressed by its commitment to providing quality community services and supporting people in need by the provision of child care services dealt with in this report.

Environmental Well-Being is enhanced. ☐ Yes ☑ No

Economic Well-Being is enhanced. ☑ Yes ☐ No

City Council’s strategic commitment to “Best Practices – Best Value” under “A City That Spends Wisely and Invests Strategically” is addressed through audits and reviews and their subsequent follow up to ensure controls are in place to protect the assets of the City and promote efficient, effective and economic services and programs.

Does the option you are recommending create value across all three bottom lines? ☐ Yes ☑ No

Do the options you are recommending make Hamilton a City of choice for high performance public servants? ☑ Yes ☐ No

ap:dt
Attachment – Appendix “A”
## Calculation of Per Diems

Subsidies paid to child care providers are based on per diem rates determined using an established formula that incorporates each provider's expenditure projections as well as the provider's licensed capacity for each age group. As such, per diem rates are different for each provider as they are based on each provider's specific circumstances.

When calculating per diems, staff often make discretionary adjustments to the formula in an attempt to allocate costs away from infant and toddler categories to pre-school and school age groups. The actual cost of care for younger age groups generally exceeds maximum per diems paid by the City. Therefore, staff consider the adjustments to be a 'weighting mechanism' to compensate providers for the high cost of infant and toddler care. However, when making the adjustments, staff do not include notes that provide the rationale for the adjustments.

While the necessity for the formula to recognize the higher cost of care for younger age groups can be appreciated, the lack of a consistent methodology and the extensive reliance on individual staff discretion could undermine the integrity of the calculation. In addition, because the calculation is not independently reviewed, errors and resulting overpayments may not be detected in a timely manner.

In January 2007, one provider's per diem rates were incorrectly calculated due to an error in the formula. As the calculation was not independently reviewed, it has remained undetected for over 17 months, resulting in a net underpayment to the provider of approximately $15,150.

### Recommendations

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<th>Recommendation</th>
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<tr>
<td>That the formula for calculating per diem rates be revised and formalized to incorporate a consistent weighting mechanism that recognizes the higher cost of care for younger age groups.</td>
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<td>That the calculation of per diem rates be independently reviewed for accuracy prior to the approval of the new rates by the Program Manager.</td>
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### Management Action Plan

- The Child Care System initiated a Business Process Review (BPR) in February 2007. Phase I of the review was completed in March 2008. Phase II, the design and implementation phase immediately followed and continues. It is estimated that phase II will be completed in Q.1 2009 at which time a report will be presented to the Emergency and Community Services Committee of Council.

- Agreed. Staff are currently revising formulas. Policies and procedures are being updated with an expected completion date of Q.2 2009.

- Agreed. Effective September 2008, a second review of per diem rates has been implemented as an interim measure until the recommendations from the Business Process Review (BPR) are reviewed and new business processes are implemented. Expected completion date of the BPR is Q.1 2009.
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<td>2.</td>
<td>Submission of Documents</td>
<td>That management enforce the requirement for the annual submission of financial statements.</td>
<td>Agreed. The program does not have the capacity at the present time to consistently enforce this requirement. These three recommendations will be integrated into the new business processes forthcoming as a result of the BPR recommendations expected to be completed Q.1 2009. Implementation of this recommendation will be dependent upon resources.</td>
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<td>The service agreement signed with child care providers requires each provider to submit annual financial statements to the City within four months of the child care provider’s year end. In addition, the provider is required to purchase general commercial liability and automobile liability insurance and submit certificates of insurance as proof of coverage to the City annually. About 50% of providers sampled have never submitted financial statements or last submitted in 2005. For those providers that have been submitting regularly, there is no indication that the financial statements are reviewed by staff and compared to the provider’s operating budgets. A comprehensive review of financial statements serves as a vital control mechanism when assessing the reasonableness of the provider’s budget on which per diem rates are based as well as an indicator of financial sustainability. None of the providers sampled had valid insurance certificates on file. Some insurance certificates showed expiry dates as far back as December 2000. There is no indication of staff follow up for providers that are not in compliance with the above requirements.</td>
<td>That, once received, financial statements be reviewed and compared to submitted provider operating budgets.</td>
<td>Agreed. See above. Implementation is expected Q.2 2009.</td>
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<td>That management enforce the requirement for an annual submission of insurance certificates.</td>
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### Evaluation of Applications for a Service Contract

3. Evaluation of Applications for a Service Contract

While a document exists that provides guidelines to child care providers on how a business plan and functional plan are developed, there are no specific criteria for evaluating a child care provider’s application. Much reliance is placed on staff's personal knowledge and subjective assessment. Without a clear decision model that defines qualification thresholds, decisions to approve or decline applications may lack transparency and consistency. In addition, staff's decisions are not always comprehensively reviewed and confirmed by a senior official.

There is also no evidence that child care providers whose applications have been declined receive written notification from the Program Manager formally advising them of the basis of the decision made.

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<td></td>
<td>Evaluation of Applications for a Service Contract</td>
<td>That a decision model that clearly defines qualification thresholds for assessing service contract applications be developed and implemented. That the evaluation of a child care provider’s application be reviewed by a peer before the finalization of a decision to approve or decline. Evidence of such peer review should be documented.</td>
<td>Agreed. This task will be identified as part of the Child Care System’s 2009 work plan with an estimated completion date Q.2 2009. Agreed. The program does not have the capacity at the present time to implement a peer review of provider applications. This recommendation will be integrated into the new business processes forthcoming as a result of the BPR recommendations. Implementation of this recommendation will be Q.3 2009. Agreed. A form letter has been created. It was ready for implementation October, 2008.</td>
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That, unsuccessful service provider applicants be provided with a written notification, signed by the Program Manager, outlining the reasons why the application was declined.
### Segregation of Duties

Responsibilities assigned to Subsidy Eligibility Workers (SEW) do not provide for an adequate separation of incompatible duties. SEW's perform duties that include intake screening, income testing, case management, the authorization of invoice adjustments and approval of payments to child care providers. In addition, except for the approval of invoice adjustments, work performed by SEW's generally does not receive peer or supervisory review.

The Business Process Review carried out by management in 2007 identified the separation of pre-screening, intake, case management and invoice approval processes as a major impediment to efficiency, teamwork and good customer service. While the need to pursue greater efficiencies and customer service is acknowledged, it is also vital to ensure that streamlined processes are designed to prevent and detect errors and irregularities in a timely manner.

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<td>4</td>
<td>Segregation of Duties</td>
<td>That consideration be given to re-assigning responsibilities for reviewing/approving child care providers’ invoices and adjustments to a member of staff not directly involved with child placement and case management.</td>
<td>Agreed. The program does not have the capacity at the present time. This recommendation will be integrated into the new business processes forthcoming as a result of the BPR recommendations. Implementation of this recommendation Q.2 2009.</td>
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### Subsidy Overpayments

Occasionally, parents continue to receive child care fee subsidies when they are no longer eligible. Usually such overpayments arise from the failure of the recipient to notify the Child Care Subsidy Program Office of a change in family income or other information impacting eligibility. When detected, such cases are referred to the Ontario Works (OW) Recovery Office which assumes responsibility for recovering the funds. As at July, 2008, there were 92 cases of overpayments totalling approximately $52,000.

A review of a sample of such cases indicated that overpayments are not adequately tracked in the OCCMS system. Amounts recorded as owing in OCCMS differ from amounts noted in the Recovery Office’s records (SDMT system), mostly as a result of repayments made by the clients. Three of the ten overpayments in the sample were not even noted in the SDMT system of the Recovery Office. There does not appear to be any communication between SEW’s and the Recovery Office regarding amounts recovered, possibly leading to inaccurate balances owing.

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<td>5</td>
<td>Subsidy Overpayments</td>
<td>That the Child Care Subsidy Program Office obtain repayment information from the OW Recovery Office on a regular basis. The balances owing should be updated accordingly in OCCMS.</td>
<td>Agreed. The existing process is time consuming for staff. Although all policies and procedures are currently being updated as part of the Business Process Review, further consultation is required with Finance and Administration, Ontario Works Overpayment Recovery, other municipalities etc. in order to develop a more efficient process. This task will be identified as part of the Child Care System’s 2009 work plan with an estimated completion time in Q.3 2009.</td>
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### Appeal Process

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<td>6</td>
<td>Clients that have been interviewed and have been assessed to be ineligible for a fee subsidy do not receive written notification from the City advising them of the basis of the decision. In addition, the applicants do not receive a letter outlining the process for appealing the decision. Rather, communication is done verbally at the time of the application interview. The Day Nurseries Act requires the Consolidated Municipal Service Manager to advise unsuccessful applicants about the appeal process. Without a written communication to the applicant, it is difficult to demonstrate that the City is in compliance with this requirement. This issue was previously raised in a review carried out by the Province for 2005.</td>
<td>That unsuccessful fee subsidy applicants be provided with a letter outlining the basis of subsidization ineligibility as well as the process for appeals.</td>
<td>Agreed. An OCCMS form letter advising all unsuccessful fee subsidy applicants of their ineligibility including the process for appeals has been created. Implementation October, 2008.</td>
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### Grandparenting Provisions

Section 66.7 of the Day Care Nurseries Act (the Act) has provisions which ensure that those parents who were recipients of fee subsidies before the introduction of the income test on January 1, 2007 will not be financially prejudiced since the inception of the new testing. Through its grandparenting provisions, parents continue to contribute the lower rates until the child enters grade 1 (i.e. six years old).

However, if a parent’s adjusted income increases by 20% or more in a year over the adjusted income as determined in the first year the parent applied for assistance under the needs testing, grandparenting will not apply from the current year onward and the parent will pay for child care in the amount determined by the formula for the income test.

In a sample of ten clients who were subsidy recipients prior to the January 1, 2007 inception of income testing, Internal Audit found two recipients for whom the 20% income increase regulation should have applied, thus eliminating the grandparenting coverage. These clients should have been contributing at the higher rate determined by the income testing methodology prescribed in the Act.

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<td>7.</td>
<td>Grandparenting Provisions</td>
<td>That the 20% increase in income rule as stipulated in the grandparenting provision of the Act be applied to all appropriate subsidy recipients. Changes in the required contributions as a result of these calculations should be implemented immediately.</td>
<td>Agreed. City of Hamilton staff received information of this change in a policy directive from the Province on December 21, 2006 with an implementation date of January 1, 2007. The Province identified 2007 as a transitional year which included ongoing questions and answers from municipalities and the Province. Interpretation of this policy change was complex and the Province fully anticipated inconsistencies in application during the transition year. Clarification of this policy was reviewed with all staff during the October team meeting with the expectation that this policy be followed immediately as the situation arises (i.e. when a client reports significant changes and/or during the client’s annual review).</td>
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ADDENDUM

The following items were noted during the course of the audit. Although they do not present internal control deficiencies, they are indicated in this Addendum so management is aware of the issues and risks and can address them appropriately.

1. **Frequency of Per Diem Reviews**
   Per diem rates paid to child care providers are reviewed at the request of the provider and upon receipt of the provider’s budget. Therefore, providers who submit updated budgets on a regular basis are paid per diem rates that estimate their current operating costs. There are several providers whose rates were noted to be significantly lower than the average because the rates were last reviewed in the year 2000. As the providers have not submitted operating budgets and financial statements in eight years, the determination of whether the per diem rates reflect the providers’ actual cost of care could not be ascertained. It is also unclear whether the procedure for rate reviews is communicated to child care providers.

Uniform per diem rates paid to private home day care providers were last set in 2005 and have not been adjusted for inflation.

_It is recommended:_
*That, for the purpose of comparing actual expenditures to budget, child care providers be required to submit operating budgets on an annual basis, regardless of whether a rate review is being requested._

_Management Response:_
Agreed. However, the program does not have capacity at the present time to implement this recommendation. As a result of the BPR process, the recommendation will be integrated into the new business processes, provided there are sufficient resources to do so. It is important to note that all service providers were notified of the rate review in 2005. Upon further investigation, it was noted that some OCCMS fields were not updated to reflect actual rate reviews for some centres.

_That management consider the best means of communicating with child care providers regarding the procedure for applying for rate reviews._

_Management Response:_
Agreed. Numerous mechanisms are already in place regarding ongoing communication with all child care providers. The development of an ‘Access to Service’ component of the new program delivery model is one of the activities currently underway as part of the Business Process Review. One of the new service model’s goals is to increase communication and access to our services.
2. **OCCMS Access Security**

Passwords to access OCCMS, the software used for the administration of child care fee subsidies, have not been changed in several years. OCCMS is not programmed to periodically prompt users for password changes. Also, the child care unit does not maintain a log that tracks the frequency of password changes.

In addition, the system does not have a pre-set password configuration that enhances password security. For example, the password structure could be designed to be alpha numeric, with a minimum number of characters and a mandatory combination of upper and lower case characters.

While the ultimate responsibility for OCCMS rests with the Province of Ontario, the City, along with other extensive users, should lobby the Province for security and utility enhancements to the system.

*It is recommended:*

*That staff in the Social Development and Early Childhood Services Division of the Community Services Department continue to lobby the Province for an enhancement to OCCMS’ access security.*

*Management Response:*

*Agreed. A request was submitted to the OCCMS user group on September 24, 2004. To date, this request has not been approved. We will continue to lobby the user group for this enhancement. In November, 2008, a policy for the local system administrator to manually reset the passwords on a quarterly basis will be implemented.*

3. **Wait List Management Strategy**

Due to the demand for fee subsidies outweighing the available funding, a wait list was implemented in June, 2008. The Wait List Management Strategy categorizes child care fee subsidy applicants into 3 major priorities based on a mix of reason for service and income criteria. As of August 2008, over 460 applicants had been placed on the waiting list. Placement of children from the waiting list is on a first-come-first-served basis whenever spaces become available. However, the Wait List Management Strategy does not provide details regarding the determination of availability of child care spaces and subsequent placement.

*It is recommended:*

*That management establish written procedures for placements from the waiting list, including a metric for determining availability of child care spaces in order to trigger active placements from the waiting list.*

*Management Response:*

*Agreed. The Wait List Management Strategy is separate from this process as it is the policy for determining the ranking of children on the wait list which is a modified first come first served basis. The Wait List Management Strategy is used to determine the order children will be removed from the wait list, not when they will be removed from the wait list.*

*The process used to determine the availability of child care spaces is part of routine caseload/budget management and is based on the analysis of the fee subsidy budget to the existing and projected year end expenditures. This calculation is carried out on a monthly basis by Management and takes into account a range of influencing factors. Program policies and procedures are currently being updated as part of the Business Process Review with the specific section on removing children from the wait list to be completed by December, 2008.*
4. **Filing**

While electronic client files in OCCMS are considered primary storage, much of the clients’ hard copy documentation (Notice of Assessments, Parent Agreements) are still stored as paper files. There does not appear to be an efficient system of maintaining paper files as several files selected for testing could not be easily located and some could not be found at all. Terminated and active clients’ files are filed together with no indexing to distinguish active files from those that are inactive.

Files contain personal application information. Loss of this information increases the risk of unauthorized use. The lack of a good filing system can have an impact on the efficiency of the operations.

*It is recommended:*  
That a filing system be developed to ensure efficient management of clients’ paper files and prevent loss of valuable information.

**Management Response:**  
Agreed. Improvements have been implemented since the audit including the separation of terminated files from active files. Staff now use hard copy sign out cards in order to keep track of all files.