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DEPARTMENT OF AUDITOR-CONTROLLER**

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May 7, 2025

TO: Kelly LoBianco, Director  
Department of Economic Opportunity

FROM: Greg Hellmold, Chief   
Office of County Investigations

SUBJECT: **IMPROVEMENT OPPORTUNITIES NOTED DURING LIMITED REVIEW  
(REPORT #IOR-2015-10649) – THIRD FOLLOW-UP REVIEW**

We completed a third follow-up review of the Local Small Business Enterprise (LSBE) Preference Program (Program) Improvement Opportunities Noted During Limited Review (Report #IOR-2015-10649). This review focused on the certification and oversight of LSBEs, which became the responsibility of the Department of Economic Opportunity (DEO) in July 2022. As summarized in Table 1, DEO has fully implemented two recommendations and partially implemented four others to strengthen LSBEs controls and business process. DEO has stated that they are working with the Internal Services Department and County Counsel to fully implement the remaining recommendations as soon as possible.

**Table 1 - Results of Third Follow-up Review**

RECOMMENDATION IMPLEMENTATION STATUS					
PRIORITY RANKINGS	TOTAL RECOS OUTSTANDING	EXEMPT FROM REVIEW	FULLY IMPLEMENTED	OUTSTANDING RECOMMENDATIONS	
				PARTIALLY IMPLEMENTED	NOT IMPLEMENTED
PRIORITY 1	2	0	1	1	0
PRIORITY 2	4	0	1	3	0
PRIORITY 3	0	0	0	0	0
TOTAL	6	0	2	4	0
				4	

For details of our review and the Department's corrective actions, see Attachment.

We thank DEO management and staff for their cooperation and assistance during our review. If you have any questions please contact me at (213) 893-0243 or [ghellmold@auditor.lacounty.gov](mailto:ghellmold@auditor.lacounty.gov), or your staff may contact Supervising Investigator Kenneth Diaz at (213) 948-2936 or [kdiaz@auditor.lacounty.gov](mailto:kdiaz@auditor.lacounty.gov).

GH:SL:KD:ec  
Attachment

c: Oscar Valdez, Auditor-Controller  
Audit Committee  
Audit Division

# LOS ANGELES COUNTY AUDITOR-CONTROLLER

Attachment  
Page 1 of 3

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DIVISION CHIEF

**OFFICE OF COUNTY INVESTIGATIONS**

*Report #F3-2015-10649*

## DEPARTMENT OF ECONOMIC OPPORTUNITY IMPROVEMENT OPPORTUNITIES NOTED DURING LIMITED REVIEW (REPORT #IOR-2015-10649) THIRD FOLLOW-UP REVIEW

	RECOMMENDATION	A-C COMMENTS
1	<p><b>Certification of Local Small Business Enterprise Vendors (Priority 1)</b> - Department of Economic Opportunity (DEO) Office of Small Business (OSB), in consultation with the Internal Services Department (ISD) and County Counsel, strengthen the Local Small Business Enterprise (LSBE) vendor certification process to provide reasonable assurance that vendors receiving preferential treatment under the LSBE program meet ordinance and program requirements, such as having a legitimate principal place of business and serving a commercially useful function (CUF).</p> <p><b>Original Issue/Impact:</b> We noted examples where LSBE vendors systematically abused the Preference Program (Program) to fraudulently obtain County business by purporting to be legitimate providers of goods and services, but serving only as pass-through entities (i.e., intermediaries or extra participants in the transaction that do not add value or serve a CUF) to create the appearance that the transactions were with a qualifying LSBE. This violates County Code Section (§) 2.204.030 and decreases opportunities for legitimate small businesses to obtain County procurement awards and jeopardizes the continued viability of the LSBE Program.</p>	<p><b>Recommendation Status: Implemented</b></p> <p>DEO OSB management, in consultation with ISD, developed an update to the County's LSBE Certification Portal (portal). The new portal notifies and requires LSBE applicants to attest that they: 1) will provide a CUF on any bid undertaken; and 2) understand there must be no conflict of interest when they submit a bid. The updated certification portal went live on September 30, 2023.</p> <p>DEO demonstrated the certification portal, and we confirmed that the website includes descriptions of what constitutes a CUF and a conflict of interest. We also reviewed DEO records which demonstrate that they conduct monthly webinars to educate both County buyers and current or prospective LSBEs about the County's LSBE program. These webinars include fraud awareness topics and guidance on identifying and addressing potential conflicts of interest.</p> <p>We confirmed that DEO staff received training on the new process after its implementation in February 2024. To reinforce understanding and support effective application, DEO conducted additional training sessions in April and May 2024. DEO also provided a copy of the training presentation and materials, which included a certification processing checklist.</p>
2	<p><b>Suspension/Revocation of LSBE Certification (Priority 1)</b> - DEO, in consultation with ISD and County Counsel, establish a process to promptly suspend and/or revoke the LSBE certifications of vendors that violate one of the Program's requirements.</p> <p><b>Original Issue/Impact:</b> The County does not have any process to suspend or revoke the LSBE certifications of vendors that violate program provisions and ordinance requirements. Non-compliant vendors retain the benefits of LSBE certification, including pricing preferences</p>	<p><b>Recommendation Status: Partially Implemented</b></p> <p>DEO OSB management indicated that, in collaboration with ISD and County Counsel, they have been drafting ordinance amendments for the LSBE Program to: 1) authorize DEO OSB to revoke an LSBE certification for non-compliance; and 2) establish an appeals process for certified LSBE vendors to challenge DEO OSB's findings.</p> <p>An update to County Code § 2.204 is currently pending the Board of Supervisors' (Board) approval. DEO anticipates Board approval by June 30, 2025.</p>

**Priority Ranking:** Recommendations are ranked from Priority 1 to 3 based on the potential seriousness and likelihood of negative impact on the Agency's operations if corrective action is not taken.

RECOMMENDATION		A-C COMMENTS
	and reduced competition. This reduced the LSBE Program's integrity.	
3	<p><b>LSBE Conflict of Interest (Priority 2)</b> - DEO, in consultation with ISD and County Counsel, establish formal conflict of interest disclosure requirements as part of the LSBE certification process, including the obligation of LSBEs to report potential conflicts, such as financial, familial, or other relationships with County procurement decision-making personnel and other County vendors. The requirements should specify sanctions for engaging in conflicted transactions and/or failing to disclose conflicts, such as revocation of LSBE certification, debarment, civil liability for false claims, and criminal prosecution.</p> <p><b>Original Issue/Impact:</b> During the LSBE certification process, the County does not put vendors on notice or make it abundantly clear that they must adhere to County conflict of interest and gratuity policies or require prospective LSBEs to disclose relationships or potential conflicts with County employees or other vendors. This reduced program integrity and accountability.</p>	<p><b>Recommendation Status: Partially Implemented</b></p> <p>DEO OSB management indicated that, in collaboration with County Counsel and ISD, they revised the conflict-of-interest disclosure as part of the proposed LSBE Certification Acknowledgment process to address outstanding concerns. The draft revisions include requiring preference vendors to disclose any potential conflicts and incorporating a section on violations and sanctions. The final disclosure will outline potential penalties for engaging in conflicted transactions or failing to disclose conflicts, including LSBE certification revocation, debarment, civil liability for false claims, and criminal prosecution.</p> <p>The updated LSBE Certification Acknowledgment form is expected to be in use by June 30, 2025.</p> <p>Our review of the draft disclosure noted that it lists various types of conflicted relationships and clearly states, in plain language, that bidders shall not have a familial or financial relationship with any County agency or representative.</p>
4	<p><b>LSBE Vendor Acknowledgment of Program Requirements (Priority 2)</b> - DEO, in consultation with ISD management, develop a process to ensure that LSBEs are informed of and agree to comply with program requirements at the time of certification and periodically thereafter, and retain documentation of the acknowledgment as part of the vendor's LSBE certification file.</p> <p><b>Original Issue/Impact:</b> The County does not require LSBE vendors to acknowledge they received, understand, and agree to comply with program requirements (e.g., that LSBEs must perform a CUF), policies on prohibited conduct, and/or sanctions for non-compliance. LSBE vendors also are not informed of or required to comply with the standard County requirement to report attempted or actual improper solicitations or procurement-related misconduct to the County Fraud Hotline. This reduced program integrity and accountability and increased the risk of improper purchases and fraud.</p>	<p><b>Recommendation Status: Partially Implemented</b></p> <p>DEO OSB has developed a new LSBE Certification Acknowledgment process that LSBE vendors must submit to maintain their status. The certification process includes an annual self-attestation, where LSBEs confirm their compliance. Every three years, a secondary certification is required, involving the submission of additional documentation and notarization of the application. This process is expected to be implemented by June 30, 2025.</p>

RECOMMENDATION	A-C COMMENTS
<p><b>5</b> <b>LSBE Program Monitoring (Priority 2)</b> - DEO management establish a risk- and activity-based program to periodically review a sample of LSBE vendors that receive County awards, to provide reasonable assurance that the LSBE Program is functioning as intended and achieving its goals and objectives. This should include determining whether vendors are performing a CUF and complying with other significant policies and program requirements.</p> <p><b>Original Issue/Impact:</b> The County does not have a systematic plan or process for monitoring LSBE compliance with policies, procedures, and ordinance requirements. Such monitoring, particularly of LSBEs that have significant growth in County procurement activity, can identify vendors abusing the program or not performing a CUF. This reduced program integrity and accountability and the likelihood that non-compliant vendors will be detected timely.</p>	<p><b>Recommendation Status: Implemented</b></p> <p>DEO OSB has implemented a risk- and activity-based procedure to periodically review a sample of LSBE vendors that have been awarded County contracts. According to DEO management, these audits are currently underway, with an initial review of 12 high-earning LSBE businesses already completed. We obtained and reviewed OSB's audit reports and supporting documentation and confirmed that DEO conducts various analyses as part of the process, including assessing whether each vendor is performing a CUF. DEO intends to expand the scope of these reviews once additional staff are hired to support this function.</p> <p>To facilitate this effort, DEO has requested a dedicated position to oversee the reviews. However, the request has not yet been approved and is scheduled for reconsideration during the Supplemental Budget Changes process.</p>
<p><b>6</b> <b>Promoting LSBE Program Integrity (Priority 2)</b> - DEO, in consultation with ISD, consider revising existing guidelines and/or developing a new policy applicable to the LSBE Program to ensure that administrative and legal remedies are pursued consistently by all County departments when an LSBE is found to have violated program requirements. DEO should also evaluate applying the new policy to other preference programs it administers.</p> <p><b>Original Issue/Impact:</b> The County does not have guidelines and/or policies applicable to the LSBE Program in place to ensure that all County departments consistently pursue administrative and legal remedies when an LSBE is found to have violated program requirements.</p>	<p><b>Recommendation Status: Partially Implemented</b></p> <p>DEO OSB reported that they have begun notifying County departments to report LSBE Program violations to the County's Fraud Hotline and have provided training materials and rosters for various training sessions they have conducted.</p> <p>Additionally, DEO, in collaboration with ISD and County Counsel, revised the preference program ordinance to strengthen language on penalties, sanctions, and DEO's authority to revoke, suspend, or deny certifications. The updated ordinance also introduces new guidelines for reporting alleged program violations.</p> <p>DEO anticipates Board approval of the new ordinance by June 30, 2025. Following approval, DEO and County Counsel plan to apply similar revisions to the Social Enterprise and Disabled Veterans Business Enterprise Ordinances as part of a phased implementation approach.</p>

We conducted our review in conformance with the International Standards for the Professional Practice of Internal Auditing. For more information on our auditing process, including recommendation priority rankings, the follow-up process, and management's responsibility for internal controls, visit [auditor.lacounty.gov/audit-process-information](https://auditor.lacounty.gov/audit-process-information).