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**New York State Office of the State Comptroller**  
Thomas P. DiNapoli

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Division of State Government Accountability

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# **Compliance With the Reimbursable Cost Manual**

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## **State Education Department Churchill School and Center**

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Report 2012-S-20

May 2014

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# Executive Summary

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## Purpose

To determine whether the costs reported by the Churchill School and Center on its Consolidated Fiscal Reports (CFRs) were calculated properly, documented adequately, and reimbursable pursuant to the State Education Department's (SED) Reimbursable Cost Manual (Manual). The audit covers the three fiscal years ended June 30, 2011.

## Background

The Churchill School and Center consists of the Churchill School (Churchill), the Churchill Center (Center), and a Development Office. Churchill provides special education services, pursuant to Section 853 of the State Education Law (Law), to children in kindergarten through 12th grade. Pursuant to the Law, schools such as Churchill receive reimbursement from SED based on the expenses reported in their annual CFRs. To be eligible for reimbursement, reported expenses must comply with Manual requirements. Churchill officials claimed approximately \$43 million in Program-related expenses during the audit period.

## Key Findings

We disallowed \$3,023,220 in claimed costs as follows:

- \$1,412,227 in compensation costs incurred by the Center and the Development Office, but charged to the Churchill School;
- \$439,527 in food, parties, gifts, and other ineligible, inappropriate, and/or insufficiently documented expenses. These expenses included \$9,709 spent on alcoholic beverages;
- \$429,729 in employee bonuses that did not comply with Manual requirements;
- \$376,597 in compensation paid to the Churchill School's Executive Director and Chief Financial Officer in excess of SED's allowable compensation levels;
- \$220,501 in unnecessary transportation costs; and
- \$144,639 in unallowable equipment depreciation expenses.

## Key Recommendations

- Review the disallowances identified in our audit, adjust Churchill's CFRs and tuition reimbursement rates accordingly, and recover overpayments as appropriate.
- SED and Churchill officials should work together to ensure that only eligible costs are included on Churchill's CFRs.

## Other Related Audits/Reports of Interest

[Bilingual SEIT & Preschool, Inc.: Compliance With the Reimbursable Cost Manual \(2011-S-13\)](#)

[Special Education Associates, Inc.: Compliance With the Reimbursable Cost Manual \(2010-S-31\)](#)

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**State of New York**  
**Office of the State Comptroller**

**Division of State Government Accountability**

May 27, 2014

Dr. John B. King, Jr.  
Commissioner  
State Education Department  
State Education Building - Room 125  
89 Washington Avenue  
Albany, NY 12234

Mr. Robert Siebert  
Executive Director  
Churchill School and Center  
301 E. 29<sup>th</sup> Street  
New York, NY 10016

Dear Dr. King and Mr. Siebert:

The Office of the State Comptroller is committed to helping State agencies, public authorities, and local government agencies manage government resources efficiently and effectively and, by so doing, providing accountability for tax dollars spent to support government operations. The Comptroller oversees the fiscal affairs of State agencies, public authorities, and local government agencies, as well as their compliance with relevant statutes and their observance of good business practices. The fiscal oversight is accomplished, in part, through our audits, which identify opportunities for improving operations. Audits can also identify strategies for reducing costs and strengthening controls that are intended to safeguard assets.

Following is a report of our audit of the State Education Department and the Churchill School and Center entitled *Compliance With the Reimbursable Cost Manual*. This audit was performed pursuant to the State Comptroller's authority as set forth in Article V, Section 1, of the State Constitution and Article II, Section 8, of the State Finance Law.

This audit's results and recommendations are resources for you to use in effectively managing your operations and in meeting the expectations of taxpayers. If you have any questions about this draft report, please feel free to contact us.

Respectfully submitted,

*Office of the State Comptroller*  
*Division of State Government Accountability*

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This report is also available on our website at: [www.osc.state.ny.us](http://www.osc.state.ny.us)

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## Background

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The Churchill School and Center (Churchill), located in New York City, is a private not-for-profit education corporation that includes the Churchill School (Churchill), the Churchill Center (Center), and a Development Office. Churchill provides special education services, pursuant to Section 853 of the State Education Law (Law), to children from kindergarten through the 12th grade classified as having a learning disability and/or speech-language impairment. The Center offers educational programs to non-Churchill students and professional development workshops to parents, teachers, and other service providers. The Development Office administers the fund-raising, endowment, marketing, special events, and alumni activities for the affiliated entities.

The New York City Department of Education (DoE), and other school districts whose students are placed at Churchill, pay tuition to Churchill based on rates established by the New York State Education Department (SED). SED develops these rates annually using the financial information that Churchill reports on its annual Consolidated Fiscal Reports (CFRs).

SED's Reimbursable Cost Manual (Manual) offers guidance to special education providers on the eligibility of reimbursable costs, the documentation necessary to support those costs, and the cost-allocation requirements for indirect expenses.

Churchill served 397 students during the 2010-11 school year and reported approximately \$43 million in Program-related costs for the three fiscal years ended June 30, 2011 (see Exhibit at the end of this report).

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## Audit Findings and Recommendations

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We identified \$3,023,220 in costs charged to Churchill that were either unsupported, inappropriate, or non-Program related.

### Personal Service Costs

According to the Manual, a provider's personal service costs (salaries and fringe benefits) must be reported on its CFRs as either direct care costs (e.g., teacher salaries) or non-direct care (allocated) costs (e.g., administrative staff salaries). During the audit period, Churchill reported \$32,575,939 in Program-related personal service costs. We disallowed \$2,262,298 of this amount, as discussed next.

#### *Unapproved Program Costs*

We identified \$1,086,340 in compensation costs charged to Churchill for non-Program-related activities during the three fiscal years ended June 30, 2011. Churchill reported \$358,636 in extra service payments to as many as 41 Churchill employees for time worked in an after-school program run by the Center – not Churchill. Similarly, Churchill charged \$400,669 and \$327,035, respectively, in compensation and other expenses for six non-Churchill employees who worked for the Center and the Development Office performing fund-raising and other non-Program-related activities.

#### *Employee Bonuses*

The Manual defines bonuses as non-recurring, non-accumulating lump-sum payments to employees, in excess of their regularly scheduled salaries, that are not directly related to the number of hours worked. Bonuses are reimbursable if they are based on merit as measured and supported by employee performance evaluations. Churchill's annual employment agreements with its employees state that bonuses will be awarded periodically to supplement employees' regular salaries. A review of Churchill's payroll records for the two fiscal years ended June 30, 2011 showed \$429,729 in bonuses to 135 and 139 employees, respectively.

Churchill officials told us that, despite the language in their employment agreements, the payments made during the 2009-10 fiscal year were not bonuses – and therefore performance evaluations were not required. They said the extra monies paid to employees during this period offset increased health insurance premiums and helped the school recruit and/or retain qualified teachers. However, Churchill officials did not have anything in writing to support this assertion. Moreover, the same officials acknowledged that similar payments made to employees during the 2010-11 year were, in fact, bonuses and that no performance evaluations were prepared for any employee that year. We disallowed the entire \$429,729 in bonus payments made during the audit period.

### *Executive Salaries*

The Manual states that reimbursable compensation (e.g., salaries and fringe benefits) for a provider's Executive Director (ED) and the Chief Financial Officer (CFO) should not exceed the "regional median compensation" paid to comparable personnel in public schools. The limits are based on geographic location, school size, and other relevant comparable data. Based on these limits, we disallowed \$376,597 of their compensation charged to the program as follows:

- For the three-year period ended June 30, 2011, Churchill reported \$322,092, \$369,927, and \$412,850, respectively, as the compensation paid to its ED. The regional median compensation for an ED during this three-year period was \$245,578, \$240,366, and \$254,385, respectively. We are disallowing the additional \$364,540 of compensation paid to the ED during this period.
- Similarly, the reported compensation paid to Churchill's CFO for the fiscal year ended June 30, 2011 was \$214,378, while the comparable regional median compensation for a CFO during this period was \$202,321. As such, we are disallowing the \$12,057 in excess compensation charged to the Program for this individual.

SED officials informed us that they have already adjusted executives' compensation to comply with the regional median limits.

### *Unallocated Costs*

According to the Manual, the compensation paid to employees who work at multiple Churchill programs or related entities (non-direct charges) must be allocated to those programs and facilities based on a fair and reasonable methodology. During the three fiscal years ended June 30, 2011, Churchill incorrectly charged salaries totaling \$2,913,336 to the Program for employees, such as maintenance and custodial staff, whose salaries should have been allocated. Based on the ratio value allocation methodology, a methodology approved by the Manual, we determined that only \$2,587,449 of these costs should have been charged to the Program. Therefore, we are disallowing the overallocation of \$325,887.

### *Recognition Awards and Stipends*

During the audit period, Churchill issued 47 service recognition awards, totaling \$41,995, ranging from \$500 to \$2,500 per employee. SED officials advised us that service recognition awards are comparable to gifts, and therefore are not expenses eligible for reimbursement. We disallowed the \$41,995 charged to the Program for these awards.

Churchill officials also paid \$1,750 in stipends to two employees to accompany students on a seven-day surfing trip to Puerto Rico. Although Churchill officials told us the stipends were not claimed for reimbursement, we found that they were in fact included on the CFR. We are disallowing these payments as they are not Program related.

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## Non-Personal Service Costs

According to the Manual, non-personal service (NPS) costs must be adequately supported and Program appropriate. Examples of relevant supporting documents include purchase orders, receiving reports, and vendor invoices. Together, these documents describe the item(s) purchased, the associated cost, and date of receipt. During the audit period, Churchill reported an aggregate of \$10,272,447 in NPS costs on its CFRs. We disallowed \$760,922 of these costs that were either unsupported or non-Program related.

### *Transportation Costs*

The DoE and other associated local school districts pay for the busing of Churchill students to and from school at the beginning and end of each school day. The buses are also available for use by Churchill between 9:30 a.m. and 1:30 p.m. to transport students to and from off-site activities. DoE officials informed us that they assign 34 school buses to Churchill each day for these purposes, and each bus transports about 10 students. DoE officials further informed us that they issue MetroCards for student use (323 active cards during our audit).

Nevertheless, Churchill officials contracted with a private bus company to transport Churchill students to and from off-site activities during school hours. Churchill officials did not disclose this unnecessary transportation expenditure on its CFRs. Instead, our review of other CFR expense categories found \$220,501 of these costs buried in the “supplies and materials” account. We are disallowing this unnecessary, non-Program-related, and incorrectly reported expense.

### *Depreciation of Grant-Funded Equipment*

For the three fiscal years ended June 30, 2011, Churchill charged the Program \$144,639 in depreciation costs for computers it purchased with non-Program monies, specifically grants provided by the Federal Individuals with Disabilities Education Act of 2004 (IDEA). We disallowed this charge because the Manual does not allow providers to claim reimbursement for depreciation expenses on equipment purchased with IDEA grants.

### *Food, Entertainment, and Personal Expenses*

The Manual specifically states that expenses of a personal nature, meals, and entertainment of officers and/or employees are not reimbursable expenses. During the audit period, Churchill charged the Program \$126,382 for food, entertainment, flowers, parking fees, and other non-Program-related expenses, including alcoholic beverages. We are disallowing this entire amount.

We also identified:

- \$64,080 charged to the Program for the rental of an apartment and associated utilities, travel allowances, and a health club membership for the ED. Churchill officials told us the apartment was provided to the ED so he could be closer to the school. (Note: The ED’s



- home address is located just 33 miles from the school);
- \$19,511 in parking garage fees for three Churchill officials including the ED, the Facility and Security Director, and the Maintenance Supervisor;
- \$66,039 charged to the CFRs for student activities already paid for by parents and for uniforms, which are ineligible for reimbursement, according to the Manual;
- \$56,973 in bank charges, including \$49,269 in credit card processing fees, which are not reimbursable per the Manual; and
- \$3,415 in expenses that were insufficiently documented.

### *Non-Audit Services*

All special education providers which submit CFRs are required to have their annual financial statements and CFRs certified by an independent certified public accountant (CPA). As such, the costs for these services are reimbursable. However, costs for non-audit services by a CPA (e.g., investment advising, consulting) are not reimbursable. Further, if the provider's independent CPA also performs non-audit services for the provider, he/she should disclose such in the supporting notes to the financial statements.

We found Churchill paid its independent CPA a total of \$48,096 to perform budget analyses, bank reconciliations and investment, accounting, consulting, and related services during the 2010-11 fiscal year. We are disallowing these charges because they are not eligible for reimbursement. We also note that the CPA did not disclose the non-audit services performed during the fiscal year as required. We have referred this CPA firm to the SED's Office of Professions for follow-up.

### *Petty Cash*

A petty cash fund provides an entity with liquid funds for minor purchases. To properly control these funds, the fund custodian should maintain paperwork describing the nature and purpose of each fund disbursement, who requested the funds, and receipts to document those purchases. At Churchill, individual fund disbursements are limited to \$25.

We reviewed 126 petty cash disbursements (totaling \$12,481) that the fund made to Churchill's Controller (who was also an authorized signatory for fund checks) and identified \$11,126 in inappropriate expenses, as follows:

- \$7,615 in stipends where the actual use of the funds and Program relationship are not adequately documented. For example, a \$2,600 check was given to the Controller supposedly to pay \$100 each to 26 teachers who were proctoring exams. There is no evidence of these individual disbursements or supporting agreements.
- We also identified \$3,511 used for personal, non-Program-related purposes such as food for parents and staff, gifts, and MetroCards for students to attend baseball games.

### *Gifts to Oversight Agencies*

According to the Manual, the cost of gifts is not reimbursable. However, we found three separate purchases of gifts, such as candy baskets, made by Churchill's Controller to the DoE employee responsible for processing Churchill vouchers. The total cost of these gifts was \$160. Not only are these gifts unreimbursable, but the DoE employee who accepted them may have violated his/her agency's ethics policies. As such, we have referred this issue to DoE's Ethics Unit.

## **Other Matters**

### *Computers Purchased with Federal Grants*

SED is the NYS conduit for Federal IDEA grants to local education agencies such as the DoE. The DoE administers and disburses these grants to schools within the NYC school district; the grants are then used to offset the costs of special education programs. During the three fiscal years ended June 30, 2011, the Churchill School received \$1,812,680 in IDEA grants. A review of the school's general ledgers showed that \$648,043 was spent to make 45 group purchases of computers, other computer equipment, and computer-related services. However, we could not determine the exact number of computers that were purchased.

We judgmentally selected and attempted to locate 210 computers (costing \$170,199) that were purchased in three of the 45 groups. We located 93 of the 210 computers at the school. Of the remaining 117 computers, we found that Churchill School officials had donated 30 (costing \$24,870) to a Catholic elementary school and nine (costing \$5,481) to a charter school. In addition, 53 computers (costing \$32,277) were transferred to a person who collects computers for distribution to schools and organizations that need them. Churchill School officials advised that they had worked with this person in the past and were satisfied that the computers were being used by the recipient schools and organizations. We interviewed him and determined that 27 (of the 53) computers were donated to a Catholic high school. The remaining 26 computers were in the trunk of his car. Thus, the School made 92 computers available for donation to other organizations.

Based on the 93 computers located at the school and the 92 computers available for donation, we accounted for 185 of the 210 computers acquired through the three group purchases we reviewed. However, we were unable to account for the remaining 25 computers that were purchased with the IDEA funds. Moreover, Churchill School officials could not provide an explanation for the 25 missing computers.

According to Churchill School officials, they donated the computers because they had technical problems with some of them, and others were inappropriate for school use. We believe that Churchill officials should have done a better job assessing academic program and information technology needs prior to purchasing the computers to help ensure their optimal use after acquisition.

DoE officials told us that they were not aware of the disposal of the computers. They also note that although Churchill officials were not required to inform them, SED guidelines do require that such items be properly inventoried, which in this case they were not.

### *Staff-to-Student Ratios and Non-Certified Teachers*

We also identified several Program-related issues, such as questionable staff-to-student ratios and the use of non-certified teachers, which appear to be contrary to the applicable SED rules, regulations, and/or formal approvals. We have referred these issues and their pertinent details to SED for programmatic assessment and follow-up, as appropriate.

## **Recommendations**

### **To SED:**

1. Review the disallowances identified in our audit, adjust Churchill's CFRs and reimbursement rates accordingly, and recover overpayments as appropriate.
2. Review the program matters pertaining to computer utilization and disposal, student-to-staff ratios, and non-certified teachers as identified. Require Churchill to develop remedial action plans, as warranted.

### **To Churchill:**

3. Ensure that costs reported on CFRs fully comply with the applicable provisions of the Manual.
4. Establish effective inventory controls over computers and comply with applicable SED guidance and approvals with respect to teacher staffing ratios and certifications.

## **Audit Scope and Methodology**

We audited the expenses reported on Churchill's CFRs for the three fiscal years ended June 30, 2011. The objectives of our audit were to determine whether the costs reported by the Churchill School were properly calculated, adequately documented, and reimbursable pursuant to the Manual.

To accomplish our objectives, we reviewed Churchill's CFRs and supporting financial records, examined audit documentation maintained by Churchill's independent CPAs, and interviewed Churchill officials and staff. We interviewed SED and DoE officials to confirm our understanding of Manual requirements. We also reviewed supporting documentation for a sample of expenses charged to the Program. The scope of our audit work on internal controls focused on those controls over personal and NPS expense transactions, and those relating to CFR preparation.

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We conducted our performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

In addition to being the State Auditor, the Comptroller performs certain other constitutionally and statutorily mandated duties as the chief fiscal officer of New York State. These include operating the State's accounting system; preparing the State's financial statements; and approving State contracts, refunds, and other payments. In addition, the Comptroller appoints members to certain boards, commissions, and public authorities, some of whom have minority voting rights. These duties may be considered management functions for purposes of evaluating organizational independence under generally accepted government auditing standards. In our opinion, these management functions do not affect our ability to conduct independent audits of program performance.

## Authority

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The audit was performed pursuant to the State Comptroller's authority as set forth in Article V, Section 1, of the State Constitution and Article II, Section 8, of the State Finance Law.

## Reporting Requirements

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We provided our preliminary audit observations to SED and Churchill officials for their review and comment. Their comments were considered when preparing this final report and are attached in their entirety at the end of the report.

SED officials agreed with our recommendations and indicated that they have taken and will take steps to implement them. Churchill officials disagreed with most of our report's recommended disallowances. Our rejoinders to certain Churchill comments are included in our report's State Comptroller's Comments.

Within 90 days of the final release of this report, as required by Section 170 of the Executive Law, the Commissioner of the State Education Department shall report to the Governor, the State Comptroller, and the leaders of the Legislature and fiscal committees, advising what steps were taken to implement the recommendations contained herein, and if the recommendations were not implemented, the reasons why.

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## Contributors to This Report

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**Frank Patone, CPA**, Audit Director  
**Kenrick Sifontes**, Audit Manager  
**Sheila Jones**, Audit Supervisor  
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### Vision

A team of accountability experts respected for providing information that decision makers value.

### Mission

To improve government operations by conducting independent audits, reviews and evaluations of New York State and New York City taxpayer financed programs.

# Exhibit

**Churchill School and Center**  
**Schedule of Submitted, Disallowed, and Allowed Program Costs**  
**Fiscal Years 2008-09, 2009-10, and 2010-11**

<b>Program Costs</b>	<b>Amount Per CFR</b>	<b>Amount Disallowed</b>	<b>Amount Allowed</b>	<b>Notes to Exhibit</b>
<b>Personal Services</b>				
<b>Direct Care</b>	\$29,399,440	\$1,854,909	\$27,544,531	
<b>Agency Administration</b>	\$3,176,499	\$407,389	2,769,110	
<b>Total Personal Services</b>	\$32,575,939	\$2,262,298	\$30,313,641	A - C, H, J
<b>Non-Personal Services</b>				
<b>Direct Care</b>	\$8,631,796	\$682,917	\$7,948,879	
<b>Agency Administration</b>	\$1,640,651	\$78,005	\$1,562,646	
<b>Total Non-Personal Services</b>	\$10,272,447	\$760,922	\$9,511,525	A, D - I
<b>Total Program Costs</b>	<b>\$42,848,386</b>	<b>\$3,023,220</b>	<b>\$39,825,166</b>	

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## Notes to Exhibit

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The Notes shown below refer to specific sections of the Reimbursable Cost Manual upon which we have based our adjustment. We have summarized the applicable section to explain the basis for the disallowance. We provided details of the transactions in question to SED and Churchill School and Center officials during the course of our audit.

- A. Section I - Costs must be reasonable, necessary, program related, and sufficiently documented.
- B. Section I.14 - Compensation for personal services includes all salaries and wages, as well as fringe benefits and pension plan costs.
- C. Section I.14.B(2)(b) - Costs of benefits for employees who provide services to more than one program and/or entity must be allocated to separate programs and/or entities in proportion to the salary expense allocated to each program.
- D. Section I.21.A - Costs incurred for entertainment of officers or employees, or for activities not related to the program, or any related items such as meals, lodging, rentals, transportation, and gratuities are not reimbursable.
- E. Section I.21.B - All personal expenses, such as personal travel expenses, laundry charges, beverage charges, gift certificates to staff and vendors, flowers or parties for staff, holiday parties, repairs on a personal vehicle, rental expenses for personal apartments, etc., are not reimbursable unless specified otherwise in this Manual.
- F. Section I.23.C - Costs of food provided to any staff including lunchroom monitors are not reimbursable.
- G. Section I.30.(3) - Costs for food, beverages, entertainment, and other related costs for meetings, including Board meetings, are not reimbursable.
- H. Section II.A.1 - Compensation costs must be based on approved and documented payrolls. Payrolls must be supported by employee time records prepared during, not after, the time period for which the employee was paid. Employee time sheets must be signed by the employee and a supervisor, and must be completed at least monthly.
- I. Section II.A.4 - All purchases must be supported with invoices listing items purchased and indicating date of purchase and date of payment, as well as canceled checks. Costs must be charged directly to specific programs whenever possible. The particular program(s) must be identified on invoices or associated documents.
- J. Section II.C.10 - A cost is reasonable if, in its nature and amount, it does not exceed that which would be incurred by a prudent person under the circumstances prevailing at the time the decision was made to incur the cost.

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# Agency Comments - State Education Department

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THE STATE EDUCATION DEPARTMENT / THE UNIVERSITY OF THE STATE OF NEW YORK / ALBANY, NY 12234

DEPUTY COMMISSIONER  
Office of Performance Improvement and Management Services  
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April 24, 2014

Mr. Frank Patone  
Audit Director  
Office of the State Comptroller  
Division of State Government Accountability  
110 State Street – 11<sup>th</sup> Floor  
Albany, NY 12236

Dear Mr. Patone:

The following is the New York State Education Department's (Department) response to the draft audit report (2012-S-20) of the State Education Department Churchill School and Center: Compliance with the Reimbursable Cost Manual.

**Recommendation 1:**

**Review the disallowances identified in our audit, adjust Churchill's CFR's and reimbursement rates accordingly, and recover overpayments as appropriate.**

We agree with this recommendation. The Department will review and make adjustments to the CFRs as noted in the report and recover any overpayments as appropriate by recalculating tuition rates. The Department notes that the tuition rate-setting methodology reduced reimbursable costs by approximately \$4.3 million for the three years ending June 30, 2011. In addition to the reduction to reimbursable costs, the Department also reduced executive compensation allocated to the education program by \$376,595 for the same three year period. We will review and consider additional information Churchill may submit in response to this report.

**Recommendation 2:**

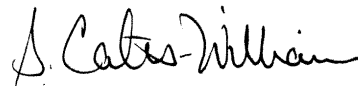
**Review the program matters pertaining to computer utilization and disposal, student-to-staff ratios, and non-certified teachers as identified. Require Churchill to develop remedial action plans, as warranted.**

We agree with this recommendation. The Department will review staff-to-student ratios and certification of teachers at the Churchill School to ensure compliance with State regulations and individualized education program (IEP) implementation and, if warranted, require corrective actions.



If you have any questions regarding this response, please contact Ann Marsh, Director of the Rate-Setting Unit at (518) 473-2020.

Sincerely,

  
Sharon Cates-Williams

c: Commissioner King  
Ann Marsh  
Maria Guzman

## Agency Comments - Churchill School and Center



April 28, 2014

Mr. Frank Patone  
CPA Audit Director  
NYS Office of the State Comptroller  
123 William Street  
New York, NY 10038

Re: Churchill School & Center, 2012-S-20

Dear Mr. Patone,

The Churchill School and Center has reviewed the recently received "Draft" audit report entitled "Compliance with the Reimbursable Cost Manual", and is submitting the following response to those audit findings.

In responding to the audit findings, we want to be clear about several key facts:

- **Churchill is uniquely chartered to serve both publically funded and private tuition students. Our other sources of funding—private tuition and fundraising—enable us to spend more on each student than the state currently allocates, resulting in an outstanding record of preparing students with learning disabilities for higher education opportunities.**
- **The taxpayers of New York did not pay the Churchill School and Center for any non-allowable costs.**
- **The state does not and never has reimbursed the compensation of any Churchill employee above the regional median for a given title, including the Head of School/CEO.**

To understand why we are able to state these facts with confidence, it is necessary to understand the history, governance and funding of Churchill.

Churchill was chartered as a private school in 1972 with a mission to educate elementary students with language-based, learning disabilities. Now in our 42<sup>nd</sup> year of continuous operation, Churchill is a highly successful K-12 program that is simultaneously a "state approved, non-public school" and a fully accredited member of the New York State Association of Independent Schools.

**THE CHURCHILL SCHOOL AND CENTER**  
301 East 29th Street New York, New York 10016  
Tel: 212 722 0610 Fax: 212 722 1387

As such, Churchill receives tuition reimbursement from the sending public school districts and the state of New York for its funded students, as well as private tuition for a number of students who are privately placed. In addition, Churchill fundraises in order to close the gap between the total tuition revenue we receive and the full cost of the programs provided to all Churchill students.

Throughout the three-year period of this audit and over much of our history, Churchill has provided to its publically funded students a comprehensive educational program that costs considerably more than what we could afford if we were to rely solely on the total funded tuition revenue provided by the school districts and the state. Churchill does not expect, nor do we receive any reimbursement for this level of expenditure.

Our additional spending on programs and support is part of what makes Churchill unique and successful, demonstrated by our outstanding record of preparing students with learning disabilities for higher education opportunities. For example, since graduating our first high school class in 2004, more than 90% of our students have achieved a Regents Diploma in four years and have continued with post-secondary education.

Having worked with us over many years, the Rate Setting Unit (RSU) of the State Education Department (SED) is very familiar with our reporting and the full scope of our spending on programs. Over the three audit years, Churchill spent \$5 million more than we were reimbursed by the state. The OSC audit identifies just over \$3 million in findings for that same period of time. Even if your findings are fully accepted by SED, there is no impact on the taxpayers of New York because those expenses are covered by private sources over the approved and funded rate levels. Therefore, there are no “over payments to recover,” as the audit report incorrectly states.

Many of our disagreements with the audit findings have to do with an interpretation of an expense, as in “employee bonuses” or “costs incurred by the Center and the Development Office.” Another disagreement is based on the wording of a provision of the Reimbursable Cost Manual (RCM) related to certain transportation expenses for school day field trips and extracurricular activities, which is clearly delineated as an “allowed” expense in the RCM.

The inclusion of executive compensation in the report is more than a disagreement over interpretation of certain wording in the Manual. In our view, this item is unfounded, misleading to the public and serves no valid OSC audit purpose. In fact, the OSC report states that executive compensation is “calculated properly, documented adequately and reimbursable,” and is reimbursed pursuant to the SED’s directions and procedures. Clearly there is no rationale for including in the audit report an item that is properly reported and appropriately reimbursed.

As with any comprehensive audit, there are a few expenses that Churchill improperly categorized or mistakenly reported in a specified year. We have acknowledged those findings and have taken the appropriate actions to ensure that our reporting on these items is changed going forward. We will continue to work with the RSU to ensure compliance with appropriate items in the OSC audit, as well as with the SED’s Rate Setting Manual.

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\* See State Comptroller’s Comments on Page 29.

Churchill has always been committed to careful stewardship of public funds and has acted with integrity consistent with the school's high standards and reputation. What follows in this response is a point by point explanation of items marked as "disallowed" in the audit. We welcome your continued feedback and consideration of our interpretations of expenses, and look forward to continuing our work with the state to provide an exceptional educational experience for children with learning disabilities.

Very truly yours,



Robert C. Siebert, Ed.D.  
Head of School



The following is The Churchill School's point by point explanation of why certain expenses have been, in our view, incorrectly marked as "disallowed" in the OSC audit report.

#### I. PERSONAL SERVICE COSTS

##### Unapproved Program Cost: \$1,086,340

- Churchill does not dispute \$199,610 of the cost, which was attributable to the Reading Initiative Program, a program Churchill makes available without charge to public school children who are reading below grade level, and to the school's Homework Club. The mistaken inclusion of the cost of the two programs was due to a procedural weakness, which we have identified and corrected. There also was one employee in one of the audited years who was mistakenly included on the CFR. This was a job coding error and we have enhanced our procedures to prevent this from happening in the future. We thank the OSC team for identifying this oversight.
- However, it is important to note that the audit team incorrectly indicated that the instructional team was not employed by Churchill; in fact, all of the team members were Churchill employees. The mistaken inclusion of the payment for the Reading Initiative on the CFR (noted above) was due to Churchill staff being paid through our regular payroll. The audit also stated that this cost was \$358,636, when in fact it was \$199,610.
- The audit report also incorrectly states that other non-Churchill employees were included on the CFR. This is incorrect in several areas.
  - First, there is only one corporation, The Churchill School and Center; all staff members are employees of this corporation.
  - Second, the Admission staff, whose salaries are partially included in this amount, were clearly employees of the school. They are split within two job codes as they had responsibilities beyond admissions, including: coordinating all IEP activities; scheduling CSE review meetings; collecting and storing student IEP's; and insuring that the programs indicated on the IEP were followed by the education staff.

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- IEP coordination is a reasonable and necessary expense in a school for children with learning disabilities; in fact the creation of an IEP defines a child as having special needs. This allocation represented \$150,670.
- \$289,270 was paid to two employees of Churchill over the three-year audit period, one whose responsibility was for the planning and coordination of all school wide events and the other whose responsibility included administrative support and the planning of all joint student and parent meetings.
  - During the second audited year, one of the staff members was eliminated and the functions were combined within the other staff member's job description. In a school of 396 students across three divisions, it is imperative that all activities are coordinated and planned through a central point of contact.
- \$446,790 was paid to the Director of Teaching and Learning and the assistant to the Director of Teaching and Learning, both Churchill employees. These two staff members were originally hired to work within the center prior to the audit years.
  - In the first audit year, the function for these two individuals was changed to develop, coordinate and support teacher training; develop teacher evaluation procedures; and ensure coordination and consistency across the curricula of the Elementary, Middle and High Schools.
  - Job title changes lagged job function and responsibility changes but were amended in 2010 to Director of Teaching and Learning and Assistant to the Director of Teaching and Learning.

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*Conclusion: Churchill acknowledges the exception of the \$199,610 addressed in the first paragraph of this section. However Churchill disputes all other amounts and findings reported in the "Unapproved Program Costs" section of the audit report.*

**Employee Bonuses: \$429,729**

- We believe that OSC is misunderstanding these transactions as being merit-based bonuses defined in section II A. (10) of the RCM. In fact, a clear reading of this section of the RCM demonstrates that these were not merit-based bonuses, which would have required employee performance evaluations. Those teachers with an unsatisfactory job performance would not have been offered employment letters from Churchill and therefore, they would not have received this compensation.
- It is important to note that the compensation in question is not a single item as stated in the report, but rather three distinct components: 1) payments given to staff to cover the cost of their health insurance increases, 2) an amount included in the professional staff's contract designed to recruit and retain qualified teachers without building up the school's salary base, and 3) a merit-based bonus in 2010/11.

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- These amounts were given out as non-recurring compensation because SED had not provided any Cost of Living Adjustments (COLAs) to our tuition rates during this period of time.
- As the school was unaware of its current and future funding (SED has not given a salary increase since 2008/09), it was prudent of Churchill not to build them into the staff's salary base. If the school had given out a built-in salary increase with no corresponding increase in tuition, this action would have violated the RCM's overarching principle of reasonableness and prudence.
- The first component of this compensation adjustment was a payment made to employees of 1.5% in 2008/09 to offset the cost of the staff's payment towards their health insurance premiums. It was not a bonus but rather a way to mitigate the impact of the significant increases in health insurance, given that employees had not received any salary increases that year.
- The second component was an amount paid to the teachers as part of their contract. As outlined above, this payment would not have been given to teachers who had poor job performance because they would not have been rehired and issued an employment letter. By definition, satisfactory job performance is all that is required for a bonus. However, the more significant aspect of this is that these were not bonuses at all—they were a component of the teachers' compensation for the year included in their contract.
  - Because of unknowns in the funding stream, we could not prudently carry these amounts forward into next year's base salary. Therefore, these payments were given as part of their annual salary preset at the beginning of the year.
  - A merit-based bonus is not preset but, rather, is determined after a certain period of time has passed and an evaluation can be performed. Therefore, these are not bonuses requiring performance evaluations.
  - The portion of these payments that was a true merit-based bonus given out in 2010/11 was based on staff evaluations and, therefore, this expense should not be disallowed as non-allowable.

*Conclusion: We believe that the OSC is misconstruing these transactions as merit-based bonuses when they are not. In addition, the very modest 1.5% increase to the base salary and the 1.5% payment is extremely reasonable and prudent under the circumstances prevailing at the time the decision was made to incur these costs.*

**Executive Salaries: \$376,597**

- Churchill continues to be confused by the inclusion of a "disallowance" for executive salaries, which were neither reimbursed nor expected to be reimbursed. This fact is stated in the audit report on page 6 in the last sentence in the Executive Salaries section. Churchill

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did not ask for reimbursement for this compensation and it was reported correctly to the state; therefore, we can only surmise that its inclusion in the report is to create the inaccurate impression that our leadership is being overcompensated relative to their peers. Nothing could be further from the truth.

- Churchill, as an independent school, competes with other independent schools for their executive team. The Churchill Board follows best practices in the compensation of their leadership and, in fact, is below the median for a peer group of similar schools.
- Churchill completely understands that the level of reimbursement by the state is capped by regional medians. However, neither Churchill nor any other independent school is in any way restricted by this cap in arriving at executive compensation levels.

*Conclusion: This finding is not valid and should be removed from the audit.*

#### **Unallocated Costs: \$325,887**

- The audit asserts that \$2,913,337 (3-year amount) of compensation for facility support staff (i.e., Day Cleaner, Evening Cleaner, Director of Facilities and Security) should be allocated using the ratio value method. This would imply that the auditors believe these costs should have been reported as agency administrative expenses on CFR-3, and allocated as shared administrative costs via ratio value. We disagree with this statement.
- First, there are no facility support Position Title Codes (PTC) in the 600 range for reporting facility support staff on CFR-3 (the 600 PTCs are the only accepted agency admin PTCs). The only acceptable facility support staff Position Title Codes are the 100 PTCs which can only be reported directly in the program columns (CFR-1) on the CFR.
- Second, the CFR Manual specifically states that Capital and related costs should be allocated based on square footage. Based on that, 85% of the cost at issue should have been charged to the school program, with 5% charged to development and 10% relating to the agency administration space shared between the two areas based on their ratio value share.
- As the school program receives 93.5% (ratio value share) of the allocated agency administration costs, the school program's total share of these expenses would be 94.35% of the total costs. Therefore, the statement that \$2,913,337 was misallocated is incorrect and should be revised to reflect the fact that only \$164,600 for the three years audited should have been allocated to the non-funded programs.

*Conclusion: The statement that \$2,913,337 was misallocated is incorrect and misleading; it should be revised to reflect the fact that only \$164,600 for the three years audited should have been allocated to the non-funded programs.*

#### **Recognition Awards and Stipends: \$41,995**

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- We disagree with the disallowance of the service recognition award payments as being unnecessary costs. Retaining qualified staff is a positive outcome for the quality of the educational services provided. This philosophy is shared by the SED, which instituted the Excess Teacher Turnover grant program, aimed at retaining teachers.
- Retaining staff, as well as teachers, also enables the continuation of services from year to year with less start-up time than would be needed with new staff. This improves the educational service and results in better outcomes for the children we serve. Towards that end, we have a policy, as many organizations do, of rewarding staff with nominal amounts for major anniversaries (5-year, 10-year, etc.).
- The \$1,750 mentioned in the report was not reported on the CFR. Therefore it cannot be disallowed and this finding should be removed.

*Conclusion: These payments have assisted us in retaining staff and improving the quality of our educational services. Therefore, these expenses are reasonable and necessary for the education program and should not be disallowed.*

## II. NON-PERSONAL SERVICE COSTS

### Transportation Cost: \$220,501

- This disallowance is incorrect on a number of levels.
  - First, Churchill does not and has not transported non-Churchill students.
  - Second, this cost has not been incurred for the transportation of students to school in the morning and home from school in the afternoon. This type of transportation is provide by the City.
  - Third, this cost is based on the transportation from school to extracurricular activities and back to school when the activity is completed.
  - Fourth, this is a reimbursable cost according to the regulations stated in the RCM, found in paragraph 11. Student Activities, subsection A.
    - **“Costs incurred for intramural activities, student publications, student clubs and other activities, to the extent such activities are normally provided by public day schools, are reimbursable direct care expenditures. Reasonable costs of class field trips during school hours and extra-curricular activities after school hours are reimbursable as direct care expenditures.”**
- Churchill concedes that it was reported in error under the incorrect line; however it was correctly reported in the “Other Than Personal Services” section of the CFR and as such would not impact the tuition rate.

*Conclusion: This disallowance is incorrect and should be removed from the report.*

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**Depreciation of Grant Funded Equipment: \$144,639**

Churchill does not dispute this finding.

**Food, Entertainment, and Personal Expenses: \$439,527**

- The \$439,527 is the consolidation of a number of items. We have listed each individual item below:
  - \$64,080 – Apartment: While there is a clause in the Head of School’s contract allowing for a health club membership, it was never utilized. Including a comment that these funds were used to pay for a membership to a health club is factually wrong.
  - While Churchill strongly believes in the need for an apartment near the school because of the many nights that are called for in the Head’s role, regardless of how far out of the city they may live, we do not dispute this finding.

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\$126,382 Food, Entertainment...Etc.

Churchill does not dispute this disallowance.

\$19,511-Parking Fees: Parking is paid for the Director of Facilities, Night Maintenance Supervisor and the Head of School.

- The Director of Facilities and the maintenance staff supervisor are responsible for the schools facilities 24 hours a day, 7 days a week. As such, they are frequently called upon to be at the school for emergencies during hours when the school would normally be closed. We believe that having this staff look for parking during an emergency is not prudent. In addition they often are called upon to run errands during school hours. It is felt that this requirement of their positions justifies a parking space to ensure the safety of the students and well-being of the facility.
- The Head of School is also required to be at the school during all hours of the day and night. Due to the time demands of the Head’s responsibilities, the Board of Trustees believes that this is a reasonable and necessary expense.

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*Conclusion: Churchill disputes this finding. We believe that being called upon to be at the facility on an as needed and urgent basis is both necessary and required. Providing a parking space in these cases does not qualify as a “perk.”*

\$66,039- Student Activities, 56,973-Bank Charges, \$3,415-Insufficient Documentation

Churchill does not dispute this finding.

**Non-Audit Service: \$48,096**

- We take exception to the disallowance of \$48,096 for non-audit services. All of the services that our accounting firm provides are either directly or indirectly related to the audit function. The RCM rule being cited in the report specifically identifies those non-audit services that are considered not allowable. None of the non-allowable services were provided to us by our accounting firm.

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*Conclusion: As our accounting firm is not performing any unallowable non-audit services and as we have provided documentation to support the amounts reported, this finding should be eliminated.*

Petty Cash-\$11,126, Flowers-\$160

Churchill does not dispute this finding.

**Other Matters****Computers Purchased with Federal Grants**

- Churchill disputes the audit report statement that the school improperly disposed of computers purchased with Federal IDEA grant monies. This is incorrect for the period audited.
- We have confirmed that the Department of Education of NYC guidelines, during the period of the audit, did not include a requirement to notify the DoE of the disposal of this equipment. Items of equipment with a current per-unit fair market value of less than \$5,000 may be retained, sold or otherwise disposed of with no further obligation to the NYSED. (NYSED does reserve the right to transfer furniture or equipment to another grantee after the grant period.)

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*Conclusion: Based on DoE guidelines, this finding is not accurate and should be removed from the report.*

**Staff to Student Ratios and Non-Certified Teachers**

- Student staffing ratios within the high school necessarily fluctuate as they do in public high schools in order to provide a comprehensive program that prepares students for post-secondary options. Core academic classes have 12 students with 2 teachers, while certain elective and/or advanced course options such as advanced studio art, graphic design or video editing, may have fewer students based on interests and college/career aspirations.
  - Mandates created by the re-authorized IDEIA require that special education students have access to challenging general education programs in order to

"prepare them for further education, employment and independent living." These courses are designed to satisfy that mandate.

- Regarding staff certification, the auditors' own comments indicate substantial progress in assuring "highly qualified" teachers in all classrooms at Churchill. Currently all elementary and middle school core academic classroom teachers are appropriately certified. In the high school, all core academic teachers are certified in their content area and most possess a "Students with Disabilities" extension to their content area certification making them "highly qualified" teachers.
  - All high school teachers certified in their content area but without the SWD extension must enroll in the necessary courses, which are offered here at Churchill through a partnership with Manhattanville College, to secure their extension.

*Conclusion: Student to staff ratios are appropriate and designed meet the IDEIA mandate that special education students have access to challenging general education programs. Churchill retains "highly qualified" teachers in all classrooms and offers "Students with Disabilities" extension training on-site through a partnership with Manhattanville College.*

#### **OSC Recommendations to Churchill:**

1. Ensure that costs reported on CFR's fully comply with the applicable provisions of the manual.

Churchill's response: As it has always done, Churchill makes every effort to ensure that all reported costs are necessary, appropriate and reimbursable according to the guidelines established by the SED.

2. Establish effective inventory controls over computers and comply with applicable SED guidance and approvals with respect to teacher staffing ratios and certification.

Churchill's response: Churchill has always been committed to maintaining tight inventory control over its equipment. These controls include but are not limited to: checking serial numbers of all equipment against invoices; scanning the bar code of all new equipment into a control program; and recording all serial numbers into the fixed asset ledger.

We have reviewed our procedures and have implemented a number of enhancements, such as dual signatures on the disposal of equipment. We will continue to review and enhance all inventory control procedures.

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Churchill thanks the OSC for their efforts during the audit and their support in ensuring that Churchill continues to provide an exceptional educational experience for children with learning disabilities.

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## State Comptroller's Comments

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1. Churchill's comments are misleading. In fact, the costs reported by Churchill on its CFR directly impact the tuition rates (as calculated by SED) that school districts pay Churchill. Reductions to CFR-reported costs could result in reductions to Churchill's SED-approved tuition rates, irrespective of the private revenues Churchill might need to pay costs not covered by its SED-approved rates.
2. We discussed our audit findings with SED officials before we issued our draft report. SED officials agreed with our interpretations of the Reimbursable Cost Manual's provisions as we applied them to our audit of Churchill's CFR. Moreover, in their formal response to our draft audit report, SED officials agreed with audit findings. If Churchill officials are unsure of the eligibility of certain expenses, they should consult with appropriate SED staff prior to claiming such costs on the CFR.
3. The language Churchill attributes to OSC is not included in our report. To the contrary, we take exception to the amounts of executive compensation paid to Churchill officials as detailed on page 6 of our report.
4. Our report accurately describes the different Churchill programs that were the subject of our audit. The distinctions between the Churchill "School" and Churchill "Center" are detailed on page 4 of our report. For those individuals described as "non-Churchill employees," there was no evidence provided to us (either during our field work or accompanying Churchill's response) proving that the individuals in question worked for the audited programs during our scope period.
5. We did not misunderstand the transactions in question. Moreover, as Churchill acknowledges, the bonuses in question were not merit-based (as otherwise required by the Manual). Although classified on Churchill's books and records as bonuses (and claimed on the CFRs as such), these bonuses were not supported by the required written employee performance evaluations.
6. Our report appropriately cites the overpayments made to Churchill's ED and CFO. As with all other special education providers receiving State funding, Churchill officials are subject to the salary caps, as noted in our report, for rate setting purposes.
7. Churchill officials are incorrect. Our report does not state that \$2,913,337 was misallocated to the Program. We state that \$325,887 of that amount was misallocated. Further, according to the Manual, the salaries of administrative personnel should be allocated based on work effort. Since Churchill does not maintain records to illustrate the actual work effort of its employees, we applied a salary allocation methodology as permitted by the Manual. Further, the square footage method cited by Churchill officials would more appropriately be used to allocate space-related expenses, such as rent and utilities.
8. Our report does not address the programmatic merit of recognition awards. However, the costs of such awards are not reimbursable per the Manual. Further, the \$1,750 cited in our report was in fact included on Churchill's CFR. Such costs might have been chargeable to the Excess Teacher Turnover grant, which is a separate funding program.
9. We deleted the reference to non-Churchill students from the report. Further, although the Manual allows costs to transport students to and from extracurricular activities, such costs must be necessary for the program. However, as detailed in our report, the DoE and

other school districts made buses available to Churchill to transport students during the school day. Consequently, the costs of a private carrier to transport students when public buses were available constituted an unnecessary, and therefore, ineligible expense.

10. As noted in our report, fees for the ED's health club membership were claimed on Churchill's CFR.
11. Routine parking for employees is not an ordinary and necessary expense of the Program, and as such, it is not reimbursable. Further, Churchill provided no evidence of emergencies that would have required employees to incur parking costs.
12. Churchill officials have not provided us with any documentation to dispute this finding. As detailed in our report, Churchill claimed costs for budget analysis, bank reconciliations, investment and other non-audit services which are ineligible for reimbursement per the Manual.
13. We revised our report wording on pages 9 and 10 after following up with SED and DoE.
14. We have referred our observations in these other Program areas to SED for the appropriate follow-up.