New York State Office of the State Comptroller
Thomas P. DiNapoli
Division of State Government Accountability

Compliance With the Reimbursable Cost Manual

State Education Department Just Kids Early Childhood Learning Center

Report 2015-S-13 December 2015

Executive Summary

Purpose
To determine whether the costs reported by Just Kids Early Childhood Learning Center (Just Kids), on its Consolidated Fiscal Reports (CFRs) were reasonable, necessary, directly related to the special education program, and sufficiently documented pursuant to the State Education Department's (SED) Reimbursable Cost Manual (Manual). The audit included the expenses claimed on Just Kids' CFRs for the fiscal years 2011-12, 2012-13, and 2013-14.

Background
Just Kids Early Childhood Learning Center (Just Kids) is a Suffolk County-based for-profit organization that is authorized by SED to provide, among other SED-approved programs, Preschool Special Education Itinerant Teacher (SEIT), Special Class (SC), and Special Class in an Integrated Setting (SCIS) programs to disabled children between the ages of three and five years. During the 2013-14 school year, Just Kids served about 803 students. Local school districts refer preschool students to Just Kids programs based on clinical evaluations. The counties pay for the preschool special education services using rates established by SED. The rates are based on the financial information that Just Kids reports to SED on its annual CFRs. The State in turn reimburses the counties 59.5 percent of the statutory rates they pay Just Kids. For the three fiscal years beginning July 1, 2011 and ending June 30, 2014, Just Kids reported approximately $53.7 million in reimbursable costs for its SED Programs. In addition to the Preschool special education programs, Just Kids also operates a day care center. Several Just Kids employees also performed services at an affiliated entity, Just Kids Diagnostic & Treatment Center. Just Kids and the Diagnostic & Treatment Center share a common ownership. This less-than-arm's-length relationship, as defined in the Manual, is disclosed in the notes to Just Kids' Annual Financial Statement.

Key Findings
For the three fiscal years ended June 30, 2014, we identified $417,994 in reported costs that did not comply with the Manual's requirements and recommend such costs be disallowed. These ineligible costs included $229,117 in personal service costs and $188,877 in other than personal service (OTPS) costs. Among the disallowances we identified were:

- $148,590 in OTPS expenses, including $117,986 for repairs, maintenance, office supplies, and utilities;
- $108,662 in employee day care discounts given to employees who were not the parents of the students enrolled in their programs;
- $70,951 for lack of time records/work product for an employee; and
- $38,800 in overstated compensation for two employees.

We have also identified certain less-than-arm's-length transactions by Just Kids that SED should reevaluate.

Key Recommendations

To SED:

- Review the recommended disallowances resulting from our audit and make the appropriate adjustments to Just Kids' reimbursement rates.
- Work with Just Kids officials to help ensure their compliance with Manual provisions.
- Re-evaluate Just Kids' less-than-arm's-length (LTAL) lease and health service transactions for reasonableness and cost effectiveness.

To Just Kids:

- Ensure that costs reported on future CFRs comply with all Manual requirements.

Other Related Audits/Reports of Interest

Milestone School for Child Development: Compliance With the Reimbursable Cost Manual (2014-S-37)
Churchill School and Center: Compliance With the Reimbursable Cost Manual (2012-S-20)

State of New York
Office of the State Comptroller

Division of State Government Accountability

December 31, 2015

Ms. MaryEllen Elia
Commissioner
State Education Department
State Education Building
89 Washington Avenue
Albany, NY 12234

Mr. Steven Held
Executive Director
Just Kids Early Childhood Learning Center
35 Longwood Road
Middle Island, NY 11953

Dear Ms. Elia and Mr. Held:

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-funded services and 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. This 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, entitled *Compliance With the Reimbursable Cost Manual*, of our audit of the costs submitted by Just Kids Early Childhood Learning Center to the State Education Department for purposes of establishing preschool special education tuition reimbursement rates. This audit was performed pursuant to the State Comptroller's authority as set forth in Article V, Section 1 of the State Constitution; Article II, Section 8 of the State Finance Law; and Section 4410-c of the State Education 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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Background

Just Kids Early Childhood Learning Center (Just Kids) is a for-profit organization that is authorized by the State Education Department (SED) to provide, among other SED-approved programs, preschool Special Education Itinerant Teacher (SEIT, code 9135), Special Class (SC, codes 9103 and 9115), and Special Class in an Integrated Setting (SCIS, codes 9160 and 9165) programs to disabled preschool children ages three through five years. For the purposes of this report, these programs are collectively referred to as the SED Programs. Based in Middle Island, New York, Just Kids provides these SED Programs to children throughout Suffolk and Nassau counties. During the 2013-14 school year, Just Kids served about 803 students.

Local school districts refer preschool special education students to Just Kids programs based on clinical evaluations. The counties pay for the preschool special education services Just Kids provides using rates established by SED. The State in turn reimburses the counties 59.5 percent of the statutory rate it pays to Just Kids. The rates are based on the financial information that Just Kids reports to SED on its annual Consolidated Fiscal Reports (CFRs). To qualify for reimbursement, Just Kids' expenses must comply with the criteria set forth in SED's Reimbursable Cost Manual (Manual), which provides guidance to special education providers on the eligibility of reimbursable costs, the documentation necessary to support these costs, and cost allocation requirements for expenses relating to multiple programs. Reimbursable costs must be reasonable, necessary, program-related, and properly documented.

Chapter 545 of the Laws of 2013 mandates the State Comptroller to audit the expenses reported to SED by special education service providers for preschool children with disabilities. For fiscal years 2011-12, 2012-13, and 2013-14, Just Kids reported approximately $53.7 million in reimbursable costs for its SED Programs. Our audit scope period focused on fiscal years 2011-12 through 2013-14.

In addition to the preschool special education programs subject to our audit, Just Kids also operates a day care center. Several Just Kids employees also performed services at an affiliated entity, Just Kids Diagnostic & Treatment Center, which provides therapeutic services for Just Kids students. Just Kids and the Diagnostic & Treatment Center share a common ownership. This less-than-arm's-length relationship is disclosed in the notes to Just Kids' Annual Financial Statement.

Audit Findings and Recommendations

For the three fiscal years ended June 30, 2014, we identified $417,994 in reported costs that did not comply with the Manual's requirements for reimbursement. The ineligible costs included $229,117 in personal service costs and $188,877 in other than personal service (OTPS) costs (see Exhibit on page 15 of this report). In addition, we identified two significant issues pertaining to related-party transations that warrant additional SED review and analysis.

Personal Service Costs

According to the Manual, personal service costs, which include all taxable and non-taxable salaries and fringe benefits paid or accrued to employees on the agency's payroll, must be reported on the provider's CFR as either direct care costs (e.g., teachers' salaries) or non-direct care costs (e.g., administrators' salaries). During fiscal years 2011-12 through 2013-14, Just Kids reported about $22.6 million in personal service costs. We identified $229,117 in personal service costs that did not comply with the Manual's guidelines for reimbursement, as follows:

Employee Day Care Discounts

Non-mandated fringe benefits are the costs of employer contributions for fringe benefits not mandated by Federal, State, or local laws. According to the Manual, examples include vacation leave, sick leave, health and dental insurance, and employer's contribution to pension or retirement plans. According to the Manual, costs will be considered for reimbursement if they are reasonable, necessary, directly related to the education program, and properly documented. On the CFRs for fiscal years 2011-12 through 2013-14, Just Kids charged $290,042 in non-mandated fringe benefits (discounted day care fees) provided to 63 employees and one non-employee. Just Kids officials advised that the discounted day care fees were a benefit intended to retain employees and to attract students to its SCIS program.

We reviewed the eligibility process for this benefit and found that it was offered to 17 individuals (16 employees and one non-employee) whose niece and/or grandchildren (rather than children) were enrolled in the Just Kids programs. We recommend that SED disallow the $108,662 that was charged to the SED Programs on behalf of the 17 individuals, since these individuals are not the parents of the children and are, therefore, not direct beneficiaries of the discount, and in one case, not an employee.

No Time Records/Work Product

The Manual stipulates that reimbursable compensation costs must be based on approved and documented payrolls. Payrolls must be supported by employee time records, which must be signed by both the employee and his/her supervisor, and completed at least monthly.

On its CFRs for fiscal years 2011-12 through 2013-14, Just Kids reported $70,951 in salary and fringe benefits for an employee who organized and sequenced student files at an offsite storage facility. However, Just Kids could not provide time records to support the employee's time and attendance during the three-year period. According to Just Kids' Executive Director, time records were neither required nor maintained because the employee was unable to maintain such records and was not required to work a normal workday schedule. The Executive Director advised that the employee, who was a full-time employee at an unrelated organization, worked only on demand, which primarily occurred at the beginning and end of the school year. To make a reasonable determination as to the time worked by the employee, we reviewed invoices related to items stored at the facility. However, the invoices were inconclusive, and, in the absence of timesheets or other time records, were insufficient to establish that work was performed by the employee. Therefore, we recommend SED disallow the $70,951 in salary and fringe benefits claimed for this employee because the expenses were insufficiently documented.

Overstated Compensation

The Manual stipulates that reimbursable compensation costs must be based on approved and documented payrolls. Payrolls must be supported by employee time records, which must be signed by both the employee and his/her supervisor, and completed at least monthly. In addition, the Manual requires entities operating approved programs to develop employer-employee agreements with written salary schedules and issue them to employees.

Just Kids shares certain employees with the Diagnostic & Treatment Center. On the CFRs for fiscal years 2011-12 and 2012-13, Just Kids claimed $42,547 and $34,089 in salaries and fringe benefits, respectively, for two shared employees. The employees each worked 20 hours per week at Just Kids and 20 hours per week at the Diagnostic & Treatment Center. One of the two employees, a payroll specialist, spent her workdays telecommuting. Just Kids maintained no employer-employee agreement to support how many hours these employees were contracted to work. When we reviewed time records for the two employees, we found that each worked 10 hours rather than the 20 hours per week claimed by Just Kids on its CFRs. Therefore, Just Kids should have claimed only half of their salaries and fringe benefits. As a result, we recommend SED disallow $38,800, ($22,922 and $15,878, respectively, for each employee) the excess salary and fringe benefits claimed for the programs we audited.

Just Kids officials claimed that the two employees often performed tasks outside of their regular work hours, and provided supplementary documentation, such as invoices, to show that one of the employees made after-hours purchases for the school and performed other duties. However, these were insufficient to show that they routinely worked more than 10 hours per week for Just Kids.

Bonuses

According to the Manual, bonus compensation shall mean a non-recurring and non-accumulating (i.e., not included in base salary of subsequent years) lump sum payment in excess of regularly scheduled salary which is not directly related to hours worked. In addition, bonus compensation is restricted to direct care employees only.

In fiscal year 2011-12, Just Kids claimed $10,704 in bonuses (salary and fringe benefits) paid to three of its administrative/executive level employees. Since these three employees were not in direct care titles, we recommend that SED disallow the $10,704 that was improperly charged to the SED Programs. Just Kids officials agreed with the disallowance and acknowledged that reimbursements should not have been claimed for the three administrative/executive level employees.

Other Than Personal Service Costs

According to the Manual, OTPS costs must be reasonable, necessary, program-related, and sufficiently documented. During fiscal years 2011-12 through 2013-14, Just Kids charged $31.1 million in OTPS expenses to the SED Programs. We identified $188,877 of those expenses that did not comply with SED's reimbursement requirements.

Expenses Not Allocated to the Diagnostic & Treatment Center

According to the Consolidated Fiscal Reporting and Claiming Manual (CFR Manual), when programs share the same geographic location or more than one State agency is served at the same geographic location, property and related costs must be allocated between the programs/State agencies benefiting from those resources. According to the Manual, costs will be considered for reimbursement if they are reasonable, necessary, directly related to the education program, and properly documented. Therefore, shared expenses, such as utilities and maintenance, are to be allocated between Just Kids and the Diagnostic & Treatment Center. For fiscal years 2011-12 through 2013-14, we found that Just Kids officials did not allocate the following expenses (totaling $148,590) to the Diagnostic & Treatment Center, and consequently, they were incorrectly allocated to Just Kids:

- $117,986 for repairs and maintenance, including $8,042 for groundskeeping services;
- $16,749 paid to the Long Island Power Authority;
- $11,754 for office supplies;
- $1,805 for telephone and Internet services; and
- $296 for a car service.

Therefore, we recommend that SED disallow the $148,590 that was allocated to the SED Programs. Just Kids agreed with our disallowance and acknowledged these expenses should have been allocated to the Diagnostic & Treatment Center.

Consulting Services

According to the Manual, costs of consultant services are reimbursable provided the services could not have been performed by an appropriately certified school officer or employee who possesses the necessary technical skills, or by SED's staff.

For fiscal year 2011-12 through 2013-14, Just Kids paid $34,865 to a consultant who, once a month, reviewed Just Kids' depreciation schedules, bank reconciliations, and general ledger accounts, as well as ensured that Just Kids' expenses were properly allocated. We noted, however, that Just Kids employed two part-time Chief Financial Officers (CFOs), whose combined work schedule equaled one full-time employee, and seven other fiscal staff. For fiscal years 2011-12 through 2013-14, Just Kids claimed $1.1 million in salaries and fringe benefits for these nine employees, approximately five full-time equivalents (FTEs). We recommend SED disallow $30,233 in consulting fees that were allocated to the SED Programs.

Just Kids officials disagreed with our disallowance. They advised that the consultant's services were necessary to maintain the integrity of the entity's financial documents. They also advised that having their financial documents reviewed by an outside entity is part of their internal control system. However, we noted that Just Kids paid its CPA firm $243,138 during the audit period for annual certifications of its general purpose financial statements and CFRs. Internal control assessments and substantive tests performed during these engagements should have provided reasonable assurance of the adequacy of Just Kids' internal controls and the integrity of its financial records. Moreover, quality assurance work could also have been performed by Just Kids' nine-member fiscal administration staff. Consequently, we concluded that work performed by the consultant was not reasonable or necessary.

Unsupported Telephone Expenses

According to the Manual, reimbursable OTPS expenses must be supported by sufficient and appropriate documentation, such as leases and invoices. On the CFRs for fiscal years 2011-12 through 2013-14, Just Kids claimed $833 in cell phone charges. We recommend that SED disallow these charges because they were insufficiently documented.

Staff Travel

According to the Manual, costs will be considered for reimbursement if they are reasonable, necessary, directly related to the education program, and properly documented. Generally, mileage incurred when travelling from work to one's home is considered a cost of commuting and thus not eligible for reimbursement. We found that Just Kids' Assistant Executive Director (AED), whose home is located between Just Kids' Lindenhurst and Middle Island sites, was reimbursed for traveling between the two sites at the end of her work day. At the beginning of the work day (generally between 8:00 a.m. and 8:30 a.m.), the AED drove 14 miles from her home to the Middle Island site. She would then leave at around 9:00 a.m. to travel 34 miles to the Lindenhurst site. At 3:00 p.m., she drove 34 miles back to the Middle Island site, spend about an hour there and then drove home. This travel itinerary allowed her to claim an additional $9,221 in mileage reimbursement.

The AED would not have been eligible to receive this amount had she traveled home from Lindenhurst and then reported to the Middle Island site the following morning. Further, we noted four days when this employee claimed a total of $99 in mileage reimbursement, although her timesheets showed she was on leave or absent those days. We find the travel to and from the Lindenhurst and Middle Island site at the end of the workday to be unnecessary and unreasonable. Therefore, we recommend that SED disallow the $9,221.

Other Pertinent Matters

Our audit also identified two significant issues pertaining to related-party business arrangements that warrant additional SED review and analysis.

Related-Party Lease Agreements

Prior to 1989, reimbursement rates for preschool special education providers were set by Family Courts. In 1989, NYS Education Law transferred responsibility for the provision of special education services from the Family Courts to local school districts, thus initiating a revised criteria for reimbursement of preschool special education providers. According to the Manual, costs incurred in a less-than-arm's-length (LTAL)[1] lease of real property transactions should be limited to the lesser of the owner's actual cost or fair market value of the rental. However, the Manual permits reimbursement at a level other than actual costs if written approval from the Commissioner's designee is provided.

In 1985, Just Kids entered into a 15-year agreement with Cam-Held Enterprises, a related party owned by Just Kids' Executive Director and its Business Director, for the lease of space at Just Kids' Middle Island site. The lease was extended/renewed in 1987 and again in 2002. The 2002 renewal extended the lease term for 15 years at an annual rental cost of $504,000 ($18 per square foot) with the caveat that the renewed lease "grandfathered" the provisions contained in the original leases. Just Kids advised us that the cost per square foot of the current lease, which will expire on August 31, 2017, is consistent with the fair market rates for the area.

For fiscal years 2011-12 through 2013-14, Just Kids' actual costs ($1.02 million) for the Middle Island site consisted of taxes, utilities, maintenance, and insurance. These costs were absorbed by Just Kids and the Diagnostic & Treatment Center. The fair market rent, based on their own analysis, was about $919,159 for the same period. However, Just Kids claimed approximately $1.94 million (the $1.02 million in actual costs plus the fair market value of $919,159) as rental costs, rather than the actual cost of $1.02 million as stipulated by the Manual, for entities that obtain written approval from SED. Consequently, Just Kids claimed $919,159 more than the property's actual costs. Just kids officials advised that the rental charges claimed on the CFRs were approved by SED's legal counsel. We recommend that SED formally re-evaluate the reasonableness of the building lease and related facility costs that Just Kids should be allowed to claim on its CFRs. Further, such re-evaluation should be completed prior to SED's approval of future lease renewals between Just Kids and Cam-Held Enterprises.

Related-Party Contracted Therapeutic Services

According to Section II.39.B(4)a of the Manual, costs incurred in LTAL health-related service transactions that are determined to be above actual documented costs of the owner shall be reimbursed only with written approval of the Commissioner obtained prior to the LTAL transaction

[1] According to the Manual, in general, a less-than-arm's-length relationship exists when there are related parties and one party can exercise control or significant influence over the management or operating policies of another party, to the extent that one of the parties is or may be prevented from fully pursuing its own separate interests.

upon the establishment of the cost-effectiveness that may result from the transaction. The Commissioner's approval may be rescinded retroactively if, based on further review/reconciliation/audit, it is determined that information used in the initial approval was erroneous, incomplete, did not fairly represent all relevant facts, data or issues, or there is inadequate supporting documentation for information/data provided and used during the approval process.

For fiscal years 2011-12 through 2013-14, Just Kids contracted with the Diagnostic & Treatment Center, a related party, to provide 125,000 hours of occupational, physical, and speech therapy services to students in the SED Programs. Just Kids and the Diagnostic & Treatment Center share a common ownership. This LTAL relationship is disclosed in the notes to Just Kids' Annual Financial Statement. On its CFRs for the three years, Just Kids claimed $15.2 million for these services. The Diagnostic & Treatment Center's actual costs for therapists was $10.9 million. This left the Diagnostic & Treatment Center with $4.3 million for other costs associated with the provision of related services, such as supervision, overhead, and administration.

Just Kids provided us with letters of approval from SED, indicating that the school's LTAL charges were cost effective for the period 1999 through 2014, because rates charged by the Diagnostic & Treatment Center were less than SED expected. However, when we analyzed the rates of other similar providers in Suffolk County, we found that, on average, their hourly charges for occupational, physical, and speech therapies were lower than the rates the Diagnostic & Treatment Center charged Just Kids for the same services.

According to Just Kids officials, the Diagnostic & Treatment Center's rates included other costs providers incur and charge to the SED-approved programs in addition to therapists' fees. Such costs include clinical supervisors' salaries and fringe benefits, support staff's salaries and fringe benefits, and certain facility-related costs. Nevertheless, until such costs are formally analyzed and reviewed, it is unclear that the rates the Diagnostic & Treatment Center charged Just Kids for services were truly cost effective. Consequently, we recommend that SED review Just Kids' cost analysis and supporting documentation used to demonstrate that the rates for therapeutic services were appropriate.

Recommendations

To SED:

1. Review the recommended disallowances resulting from our audit and make adjustments to Just Kids' reimbursement rates as appropriate.

2. Work with Just Kids officials to help ensure their compliance with Manual provisions.

3. Re-evaluate Just Kids' LTAL lease and health service transactions for fairness, reasonableness and cost effectiveness.

To Just Kids:

4. Ensure that costs reported on the future CFRs comply with all Manual requirements.

Audit Scope and Methodology

We audited the costs reported on Just Kids' CFRs to determine whether they were properly documented, program related, and allowable pursuant to SED's Manual. The audit included claimed expenses for fiscal years 2011-12 through 2013-14.

To accomplish our objective, we reviewed the Manual and the CFR Manual, Just Kids' CFRs, and relevant financial records for the audit period. We also interviewed Just Kids officials, staff, and independent auditors to obtain an understanding of their financial and business practices. In addition, we assessed a judgmental sample of reported costs to determine whether they were supported, program appropriate, and reimbursable. Our review of Just Kids' internal controls focused on the controls over Just Kids' CFR preparation process.

We conducted our performance audit in accordance with generally accepted government auditing standards. These 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 during our audit 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

The audit was performed pursuant to the State Comptroller's authority as set forth in Article V, Section 1 of the State Constitution; Article II, Section 8 of the State Finance Law; and Section 4410-c of the State Education law.

Reporting Requirements

We provided draft copies of this report to SED and Just Kids officials for their review and formal comment. We considered their comments in preparing this final report and attached the comments to the report. In their response, SED officials agreed with our recommendations and indicated that they would take certain actions to address them. Just Kids officials, however, disagreed with some of our report's findings. Our rejoinders to certain Just Kids comments are included in the report's State Comptroller's Comments. Just Kids officials also included a lengthy set of attachments with their response. Those attachments are not included in this report. However, they have been retained on file at the Office of the State Comptroller.

Within 90 days of the final release of this report, as required by Section 170 of the Executive Law, the Commissioner of Education 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.

Contributors to This Report

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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

Just Kids Early Childhood Learning Center
Summary of Submitted and Disallowed Program Costs
for the 2011-12, 2012-13, and 2013-14 Fiscal Years

Program Costs	Amounts Submitted Per CFR	Amounts Disallowed	Amounts Remaining	Notes To Exhibit
Personal Services				
Direct	$19,401,807	$182,263	$19,219,544	
Agency Administration	3,195,784	46,854	3,148,930	
Total Personal Services	**$22,597,591**	**$229,117**	**$22,368,474**	A - C, G
Other Than Personal Services				
Direct	$29,640,439	$114,361	$29,526,078	
Agency Administration	1,478,407	74,516	1,403,891	
Total Other Than Personal Services	**$31,118,846**	**$188,877**	**$30,929,969**	A, D - F, H
Total Program Costs	**$53,716,437**	**$417,994**	**$53,298,443**	

Notes to Exhibit

The following Notes refer to specific sections of SED's Reimbursable Cost Manual used to develop our recommended disallowances. We summarized the applicable sections to explain the basis for each disallowance. We provided the details supporting our recommended disallowances to SED and Just Kids officials during the course of our audit.

A. Section II - Costs will be considered for reimbursement provided such costs are reasonable, necessary, directly related to the special education program, and sufficiently documented.
B. Section II.13.A.1 - Entities operating approved programs shall develop employer-employee agreements with written salary scales and issue them to employees.
C. Section II.14.A.10 - Bonus compensation shall mean a non-recurring and non-accumulating (i.e., not included in base salary of subsequent years) lump sum payment(s) in excess of regularly scheduled salary which is not directly related to hours worked. In addition, bonus compensation is restricted to direct care titles/employees only.
D. Section II.14.A.2 - Costs of consultants' services are reimbursable provided that the services could not have been performed by an appropriately certified school officer or employee who possesses the necessary technical skills or by SED's staff.
E. Section II.39.B(4)a - Costs incurred in less-than-arm's-length (LTAL) purchase of health related service transactions that are determined to be above actual documented costs of the owner shall be reimbursed only with written approval of the Commissioner obtained prior to the LTAL transaction upon the establishment of the cost-effectiveness that may result from the transaction. The Commissioner's approval may be rescinded retroactively if, based on further review/reconciliation/audit, it is determined that information used in the initial approval was erroneous, incomplete, did not fairly represent all relevant facts, data or issues, or there is inadequate supporting documentation for information/data provided and used during the approval process.
F. Section II.41.B.4 - Costs incurred in an LTAL lease of real property transactions shall be reimbursed based on owner's actual cost or fair market value, whichever is less.
G. Section III.1.A - Compensation costs must be based on approved, documented payrolls. Payroll 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.
H. Section III.1.D - 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.

Agency Comments - State Education Department

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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November 10, 2015

Mr. Frank Patone
Audit Director
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Division of State Government Accountability
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Albany, NY 12236

Dear Mr. Patone:

The following is the New York State Education Department's (Department) response to the draft audit report, 2015-S-13, Compliance with the Reimbursable Cost Manual: Just Kids Early Childhood Learning Center (Just Kids).

In addition to the actions that will be taken in response to the specific recommendations described below, the Department will closely examine the circumstances that led to the findings described in the audit report. This examination will include an assessment of the programmatic oversight and fiscal management employed at Just Kids, and will be a factor in the consideration of the continued approval of this provider and the corrective action or enforcement actions that may be warranted.

Recommendation 1: Review the recommended disallowances resulting from our audit and make the appropriate adjustments to Just Kids' reimbursement rates.

We agree with this recommendation. The Department will review the recommended disallowances as noted in the report and make adjustments to the reported costs to recover any overpayments, as appropriate, by recalculating tuition rates.

Recommendation 2: Work with Just Kids officials to help ensure their compliance with Manual provisions.

We agree with this recommendation. The Department will continue to provide technical assistance whenever requested and will strongly recommend that Just Kids officials take advantage of our availability to help them better understand the standards for reimbursement as presented in Regulation and the Reimbursable Cost Manual. In addition, Consolidated Fiscal Report (CFR) training is available at six locations across the State and online on the Department's webpage. The training is recommended for all individuals signing CFR certification statements, namely Executive Directors and Certified Public Accountants, and is required for preschool special education providers upon approval and reapproval. Furthermore, the Department intends to require that the training be mandatory for all providers.

Recommendation 3: Re-evaluate Just Kids' less-than-arm's-length lease and health service transactions for fairness, reasonableness, and cost effectiveness.

We agree with this recommendation.

If you have any questions regarding this response, please contact Suzanne Bolling, Director of Special Education Fiscal Services at 518/474-3227.

Sincerely,

Sharon Cates-Williams

Sharon Cates-Williams

c: James P. DeLorenzo
Suzanne Bolling

Agency Comments - Just Kids Early Childhood Learning Center

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December 18, 2015

VIA E-MAIL & OVERNIGHT MAIL

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Re: Just Kids Early Childhood Learning Center // 2015-S-13
Compliance with the Reimbursable Cost Manual

Dear Mr. Patone:

We have reviewed the Draft audit findings of Just Kids Early Childhood Learning Center ("Just Kids") for audit years 2011-12, 2012-13 and 2013-14 as referenced above and gratefully acknowledge the revisions made based upon our explanation of items identified by the auditors in the preparation of the preliminary report and the materials provided in support of the restoration of certain preliminary disallowances as discussed during the exit conference with OSC representatives. We further acknowledge the continued efforts by OSC representatives to re-analyze and re-review documentation in support of the challenges we have made which, as we understand, will be reflected by further revisions to this Draft, specifically as related to OTPS repairs, maintenance, office supplies, now-allowable food expenses and consulting services. We must, however, renew our challenges to certain findings we believe will remain included in the final report as set out below and request reconsideration of the information in finalizing the audit.

* Comment 1

Personal Services Costs

Employee Day Care Discount

We challenge the auditors' assessment that Just Kids offered an employee benefit (a day care discount) to certain employees the "benefit" of which did not inure to the employee. As we explained at some length during the auditor's field work, Just Kids faces significant challenges in attracting and retaining qualified staff and personnel. Just Kids offers the "day care discount" to its employees as an incentive to continuing their employment. Just Kids allowed members of the employee's immediate family to enjoy the employee benefit much as other employers offer health insurance coverage through family plans, or college tuition savings programs - - the direct benefit being enjoyed by the employee, but the indirect beneficiary being of the employee's

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*See State Comptroller's Comments, Page 31.

choosing. We are unaware of any restriction under law preventing the employee from naming another family member as beneficiary of the employee's benefit. Employees retain the right to designate beneficiaries in other contexts such as retirement and life insurance plans. Just Kids viewed the day care discount in a similar context, allowing the employee to designate the beneficiary of the benefit whether the employee's own child, or grandchild. We do not agree with the auditors' assessment that the designated beneficiary was required under law or public policy to be the employee's own child so long as the beneficiary was within the employee's immediately extended family. This view is consistent with NYSED's own approach to determining "related party transactions" - - that immediately extended family members such as grandchildren, nieces and nephews, are considered related parties. OSC's own "Internal Control Questionnaire" defines immediate family to include grandchildren and other members. Accordingly, Just Kids used the identical standard in determining who within an employee's "immediate family" could be the designated beneficiary of the employee benefit.

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Comment
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Not insignificantly, this employee benefit also works to assure the "general education" complement to Just Kids' integrated classrooms - - a challenge NYSED recognizes as an impediment towards fuller integration throughout the State. Point in fact, the employees accepted the discount as a benefit, recognized it as such, and were incentivized to remain with Just Kids. That Just Kids was also able to continue to operate its integrated programming with these employee-discounted general education children is an additional benefit.

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Just Kids would also recall for the auditors that the staff contribute a total of $4,554.00 - - their portion of the daycare costs which equals the amount of the benefit contribution. The sum of both the daycare payment and the value of the discount is considered "offsetting revenue" under the rate methodology, effectively reducing the School's tuition rate and, thus, the burden to the State. Clearly, it is ultimately the State that realizes the true benefit of this discount.

Time Records/Work Product

To clarify, the Executive Director did not suggest to the auditors that time records were not required to be kept by the employee who was responsible for organizing, sequencing and retrieving student files at an offsite storage facility as record/storage supervisor, but rather, that the individual was unable to maintain time records as a consequence of certain personal challenges. Just Kids attempted to make "reasonable accommodations" for these challenges, but was unsuccessful in obtaining the required time records. However, Just Kids was able to substantiate the employment activities through the series of attestations from the owner of the storage sites, emails/phone requests and photographs reviewed by auditors which are testament to the completion of storage tasks, document retrieval and related activities - - the full extent of which are reflected in the job description, retrieval procedure and visual confirmation of the maintenance of the storage system. Taken together, we believe these documents sufficiently support the work performed and the restoration of the disallowance.

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More specifically, as reflected in the job description, the assigned tasks were not required to be completed within a standard workday (9-5). Rather, the assigned tasks were required to be

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completed by the agency's next day of operation, ostensibly off-hours. Accordingly, that the employee was not observed by the auditors upon site visit does not compel the conclusion that the work was not generally requested and performed on an "as needed" basis. Importantly, a representative of the audit team toured the off-site storage facility with the Executive Director and can attest to the challenges presented by a mere request to retrieve a student's file.

We must also clarify that the employee did not work "primarily…at the beginning and end of the school year.", as the auditors suggest, but rather throughout the entirety of the school year, as stated above, outside the standard school day.

* Comment 6

Compensation

Just Kids appreciates the thoughtful consideration given by the auditors to the volumes of documentation provided in support of the two employees referenced in this finding. We have revised our recordkeeping protocols to address the auditors' concerns around the adequacy of time records.

Just Kids also appreciates the overall presentation of this and related findings by the auditors.

Bonuses

While we disagree with the auditors' assessment that the award was a bonus, Just Kids has improved its bonus award protocols, consistent with the auditors' finding which relates to only one of the three audit years. It should be noted that since the 2011-12 school year, no bonuses have been awarded. To clarify, Just Kids treated the award as deferred compensation and not a bonus requiring performance evaluation support.

* Comment 7

Other than Personal Service Costs

Consulting Services

Just Kids renews the challenge to the auditors' assessment that the services of a fiscal consultant were neither reasonable nor necessary.

First, by way of clarification, while Just Kids does employ two individuals who are both coded 603 for cost reporting purposes, as directed by the CFR and RCM, neither of these individuals is the CFO - - rather, one individual is employed as the Director of Business with a specific set of responsibilities, while the other holds the title of Controller and performs certain activities which focus on the revenue and reporting components of Just Kids' fiscal operation as distinguished from the expense component. These individuals constitute the "core" of the Just Kids' fiscal office and together represent less than 1 FTE. In addition, the auditors had initially miscalculated the number of fiscal staff. We appreciate the auditors' acknowledgment that, in

* Comment 8

* Comment 9

fact and as reported on the CFR, the total FTE's of all fiscal staff, including position 603, is 4.475 (2011-12), 5.215 (2012-13) and 4.914 (2013-14).

As we shared with the auditors, mindful of the importance of a strong fiscal infrastructure supported by sound fiscal policies, the Executive Director engaged the services of a fiscal consultant to review the integrity of the Just Kids' fiscal internal controls and protocols on an ongoing basis, in furtherance of the school's required risk assessment procedures, to identify potential weaknesses and to make recommendations for improvement. Importantly, all public school districts engage individuals to provide these services under the titled position "claims auditor". As the consultant's engagement letter provided to the auditors reflects, these services included review and consultants' assessment of monthly reconciliations of financial data, analysis of inter-company transactions, making recommendations to improve reporting capabilities and to strengthen internal controls. The "outside" consultant provided the objectivity contemplated by rigorous risk assessment protocols and necessary to assure accuracy in reporting. These activities were not duplicative of any activity in which the Just Kids' fiscal staff were engaged and were complementary services essential for any program and especially for an operation the size of Just Kids.

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Comment
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We also believe that the auditors have mischaracterized the services of the agency's CPA firm as resembling, if not duplicating, the services of the consultant. As the auditors are aware, accounting firms are constrained to provide specific services such as certification of the CFR or preparation of the financial statements. While these discrete services involve acknowledgement of the agency's internal protocols, the certification process does not include any in-depth review of the integrity of protocols so much as an acknowledgment that the protocols exist. At no point do accounting firms test the integrity of fiscal policies or procedures, conduct risk assessments – beyond the information provided on the agency's general ledger or statements. Were that the case, we would suggest, there would be no need for OSC or NYSED to call for more rigorous standards for the accounting firms engaged by the preschool special education sector as both offices have done in innumerable reports, statements and presentations.

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Comment
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In fact, the independence of an accounting firm would be compromised were representatives to provide "consulting" as well as accounting services.

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Comment
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Select Telephone Expenses

Just Kids reasserts its challenge of a disallowance for certain cell phone charges, requesting reinstatement of costs incurred by a specific staff person who agreed to be a "pioneer" for Just Kids when one JKAP classroom - - 6 children with a diagnosis of autism and 6 typically developing children in a fully inclusive classroom - - was opened on the far-east end of Long Island on November 1 of 2008. Children with an autism diagnosis were traveling for hours to attend special education pre-school programs and the County of Suffolk was anxious to look for a provider willing to serve these children closer to their home.

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This staff person was one of Just Kids' "expert" teachers with a long-standing employment relationship with Just Kids. She agreed to travel the extended distance and we were thrilled to have a unique individual to carry our "philosophy" and program structure. She engaged the community and immersed herself in her daily classroom but ALSO developed a workable protocol for a remote site that still required supervision and oversight.

In fact, the Just Kids' website lists her cell phone number as a contact for others to call. Her cell phone was her only means of communication since the Mattituck school district does not supply phone service to our program. In fact, phone service to the classroom through traditional means (Centrex) would have been cost prohibitive. (See: Phone Bills).

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Comment
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Staff Travel

Just Kids reasserts its challenge of the auditors' assessment that travel by the school's Assistant Executive Director (AED) to and from the Lindenhurst, Baldwin, Mattituck, Hampton Bays, Shirley, and Middle Island sites at the end of the workday is both unnecessary and unreasonable. As shared with the auditors, by way of context, the Executive Director insists that the Assistant Executive Director meet with him at the beginning and at the conclusion of each work day to debrief, discuss staffing issues, report on the day's operations and otherwise share program information. While other members of management are already available for such discussions at the Middle Island site, the responsibilities of the AED require that she be present at a number of satellite sites, and is, therefore, only available to the Executive Director at the Middle Island location before or at the completion of the performance of her responsibilities at the satellite sites. Her presence at the Middle Island location is vital to assuring quality programming through constant interaction with the Executive Director and the Controller, both of whom are present at the Middle Island site.

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Comment
14

Just Kids challenges, more specifically, the auditors' determination that only a single daily meeting with the Executive Director and other members of the Just Kids' management team is warranted and, therefore, results an allowable expense. The frequency of staff meetings is a programmatic decision reserved to the Executive Director. Importantly, Just Kids had recently completed a program audit by NYSED in which the program received accolades for its quality of program <u>and</u> management. It is awkward now, then, that NYSED program would support a management strategy which ensures quality programming even as the auditors deem the strategy and associated costs to be "unreasonable".

In fact, the AED engages two very discrete sets of personnel during her time at the Middle Island site. In the morning, she engages the teachers, clinicians and other personnel who are on site in advance of student arrival. At the end of the AED's work day, as need requires, she returns to Middle Island to meet, as indicated above, with management staff who remain at the school after the teachers/clinicians' work day has long since ended. Accordingly, the AED is engaged in two separate tasks – one of which cannot be substituted or satisfied by the performance of the other. Importantly, the AED would return to the Middle Island location to resolve pressing issues or participate in discussions with other management personnel.

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Other Pertinent Matters

Just Kids vigorously challenges both the propriety and the validity of that portion of the Draft Audit which identifies two issues pertaining to fully disclosed and NYSED approved related party business arrangements as warranting additional NYSED review and analysis.

In the February 3, 2015 notice to Just Kids, the Office of the State Comptroller set out its general protocol objective; more specifically "(to) focus on whether the costs and other required data submitted by Just Kids…to the State Education Department on its Consolidated Fiscal Reports for purposes of rate-setting and state reimbursement were properly calculated, adequately documented and allowable under the State Education Department's guidelines, including the Reimbursable Cost Manual." The notice cites Section 4410-c of the Education Law, in part, as authority for the audit. When read together, both the statutory authority and OSC's own audit protocols define the legitimate parameters of the auditors' review. If the State Education Department's "guidelines" are determinative, as reflected in the OSC's own protocol, then State Education Department actual engagement, review and decisions relating to the appropriateness of specific costs, are undeniably determinative.

* Comment 15

Here the State Education Department was not only consulted but fully engaged in determining the propriety of each of the two arrangements identified in the report. At the conclusion of each review, the State Education Department determined the costs were properly identified, properly reported and, thus, allowable. The auditors have exceeded the parameters of both the statute and their own audit protocols by challenging the propriety of costs which NYSED has determined to be proper, effectively substituting NYSED's judgment with its own. Such an overreach is in itself inappropriate and compels reconsideration of the issues in substance and in form.

* Comment 16

Just Kids has provided volumes of correspondence and materials which reflect the full measure of NYSED's review and analysis. Clearly, NYSED has, in fact, conducted a full review and carefully considered each of the identified issues and has formally documented its determinations of approval.

As relates to one specific arrangement, upon careful review, NYSED's Office of Counsel recognized the propriety of the transaction as a matter of law and approved all costs associated with the arrangement. As to the second arrangement, NYSED conducted a series of reviews at regular intervals, testing and retesting the underlying assumptions upon which it determined the arrangement to be legitimate and cost effective, and therefore allowable under the RCM. Thus, this section of the report is unauthorized, inconsistent with NYSED's own determinations and accordingly, should be struck in its entirety.

* Comment 17

While Just Kids is fully cognizant of the OSC's authority to conduct audits in general, and of special education programs more specifically (Article V, Section 1 of the State Constitution; Article II, Section 8 of the State Finance Law; and Section 4410-c of the State

Education Law), the scopes of such audits are not boundless. Even where the Court has recognized that the OSC has the power to audit expenditures of state funds which have been approved by another state agency (City of New v. State of New York, 40 N.Y. 2d 659, 389 N.Y.S. 2d 332) the state approval was found not binding upon the Comptroller **only** in the limited instance where the approval was without legal authority and where no particular administrative expertise was necessary. Here, NYSED was fully vested with the authority to conduct full reviews and analysis of both related-party arrangements and to make a binding decision relating to each. In fact, the RCM requires the consent of the Commissioner in such transactions which in turn, requires a comprehensive review process and analysis and not a mere administrative endeavor. The OSC, then, cannot arbitrarily and capriciously discard those legally binding decisions made by the NYSED, and especially not within the context of an audit whose protocols focus on whether costs were properly calculated, adequately documented and allowable by NYSED which is clearly evident by NYSED's well-documented own review process.

* Comment 18

OSC's overreach, then, is unsupported by law or regulation and we respectfully request the deletion of this portion of the draft, as a matter of law.

* Comment 19

Just Kids also challenges the method by which the auditors conclude that the certain related-party business arrangements warrant additional SED review and analysis. Specifically, Just Kids asserts that the auditors' summary and description of the arrangements, as well as the analysis upon which the auditors base their conclusions, are flawed and inaccurate, as detailed below:

* Comment 20

Lease Arrangements

As the auditors acknowledge, the Reimbursable Cost Manual permits reimbursement of leasehold costs at a level other than the actual cost to the owner upon written approval from the NYSED Commissioner's designee. However, upon consideration of volumes of correspondence between Just Kids and representatives of NYSED Rate Setting Unit and the Office of Counsel, the auditors effectively reject the well documented approval as lacking specificity. Clearly the auditors have ignored the clear and convincing language of the correspondence.

As early as 1992, Just Kids actively engaged NYSED by asserting the propriety of the real property rental agreement between Gordon-Held and Cam-Held Enterprises, specifically as it related to the application of the Reimbursable Cost Manual's prescription that costs incurred in less-than-arm's length lease of real property be reimbursed only to the extent of owner's actual cost or fair market value, whichever is less (See: Held to Galto, March 3, 1992; Iselin to Norlander, April 6, 1992). As reflected in the July 9, 1992 Hamel to Held correspondence, the full amount of the rent expense was deemed an allowable cost, based upon careful review by NYSED's Office of Counsel and consideration of the "grandfathered" nature of the rental agreement - - that the lease arrangement preceded the imposition of any restriction by the RCM. NYSED Counsel concurred with prior NYSED determinations yet again in 1996 when it formally stated that the lease was "grandfathered" and the costs associated were fully allowable.

* Comment 21

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NYSED's position remained fully supportive of the lease arrangement again in 2002 when Counsel advised that the "grandfathered" status of a pre-existing lease continued even where an option to renew is exercised (See: Ahearn to Madeiros). Most recently, in correspondence dated March 14, 2002, NYSED advised that the "grandfathered status" of a 2002 rider and amended lease would extend until August 31, 2017 and potentially, beyond, as a matter of law, so long as the original provisions of the lease remained substantively unchanged.

* Comment 22

The auditors, without any legal basis, reject the legal analysis of the Office of Counsel and further assert that the written approval granted based upon that analysis is not specific enough to extend to the current lease arrangement. The specificity of the approval is undeniable - - the grandfathered status of the lease would extend at least until August 31, 2017. It is unfathomable that any more specificity could have been provided. Plain language must be accorded full value.

* Comment 22

While the auditors appear to acknowledge the decades-long engagement by NYSED on the one hand, they appear, on the other hand, to minimize the importance of the demonstrated heightened level of awareness by both NYSED and Just Kids as reflected in the correspondence between NYSED and Just Kids at regular intervals.

* Comment 22

The very nature of "grandfathering" as a legal concept is to take exception to a general law based upon the preexistence of a set of unique facts. Here, the lease between the related parties pre-existed the set of laws governing the reimbursement of preschool special education programs. Accordingly, NYSED's Counsel's office was constrained to recognize the lease as a matter of law, and to allow associated costs.

* Comment 23

Moreover, legal authority notwithstanding, the Just Kids' lease arrangement is further supported by rental studies conducted by Just Kids at the request of NYSED - - in furtherance of its own assessment of the arrangement. These studies shared with the auditors and attached for reconsideration attests to the true market value of the property as distinguished from whatever source the studies relied upon in making their determination.

* Comment 24

Based on the totality of the compelling documentation attesting to the propriety of the lease agreement and its associated costs, it would appear the auditors' intention to make NYSED sensitive to the issue is, at best, misplaced and unwarranted and, at worse, salacious.

It is also important to note that an additional benefit of the lease arrangement is realized through the allocation methodology itself. Under the methodology, 35% of all leasehold costs are allocated to the D & T Clinic, based on utilization. Were the space currently allocated to the D & T Clinic which "houses" the clinicians who are contracted by at the School to provide services allocated instead to the School, as an appropriate facility cost, the net effect would, in fact, be an increase in cost to the School and, subsequently, to the State.

* Comment 25

Contracted Therapeutic Services

We take further exception to the auditors' challenge to the propriety of the contractual arrangement between Just Kids and the Article 28 Diagnostic and Treatment Center for the purchase of therapeutic services, and the recommendation that NYSED "review" the proposed cost effective analysis and supporting documentation". We object to the intimation that the acknowledged "letters of approval by SED" are somehow suspect or insufficient to demonstrate compliance with the RCM. Here again, we are concerned that the auditors may be replacing formal NYSED determinations based on well-reasoned analysis with its own flawed assessments.

More specifically, the auditors claim to have performed an analysis of "other similar providers" in Suffolk County and found the cost per hour for certain therapeutic services was significantly less than that "charged (by Just Kids) to the SED program". As the supporting documentation reviewed by NYSED time after time reflects, the true comparison is <u>not</u> cost per hour to Just Kids' charge, as such a comparison ignores the special features of this unique arrangement with the D & T Clinic; specifically, for example, that the charge to the School by the D & T Clinic is <u>only</u> imposed upon the actual delivery of the service, contrasted with other "similar providers" which employ clinicians effectively compensating those staff through salary regardless of whether the service is provided. The auditors concede that their analysis did not include consideration of this glaring difference. Moreover, the charge to the School by the D & T Clinic embraces several components which are <u>not</u> reflected in a "similar providers'" hourly rate such as costs associated with supervising the clinicians - - costs which "similar providers" allocate to supervisory staff and "away" from the clinical staff's hourly rate. A "truer" and more appropriate analysis than the "hourly rate" comparison conducted by the auditors, then, would be an analysis that combines "similar providers'" hourly rates with the cost of all other associated activities which <u>support</u> that clinical service.

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Comment
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The D & T Clinic engages in a number of activities to ensure all services and administrative aspects of the adequacy and quality of services provided meet the NYSDOH and NYSED standards of care. These medical and support services are not separately charged to the School but are included within the clinicians' charge. Costs which are embraced by the D & T Clinic charge to the School include:

- Oversight by an appointed medical director with the training, experience and administrative ability to assume responsibility for all medical and rehabilitative services;
- Daily medical consultation with staff focused on therapeutic interventions, health status of medically fragile children, assistance with drug management and administration, nutrition consultation and other related support;
- Provision of continuing care by the same therapeutic practitioners to allow for constant review of child progress in a medical model of support. This model enables the sorting and allocation of treatment to children in a system of priorities designed to maximize the quality and efficiency to address the needs of children;

- The establishment and implementation, in consultation with qualified social workers, plans for care that are consistent with available community and center resources to provide for the provision of social work, psychological and educational services that may be necessary to meet the treatment/IEP goals of its patients/clients. Unlike social workers in a school-based model, all children's and family needs are developed and supported within the context of a medical and therapeutic system of care rather than a custodial model in most school settings. This difference in care supports long-term developmental issues facing the child and family over quite possibly a life-time. Documentation of this nature serves the State in the continual transitions many children face medically, educationally, psychologically, and vocationally;
- Medical oversight of all therapeutic staff are assigned by clinical privileges, and on-going review of appointments based on quality and efficiency of services;
- Maintenance of a written quality assurance program following Article 28 requirements that includes a planned a systematic process for monitoring and assessing the quality and appropriateness of care and clinical performance on an on-going basis functioning in a continuous improvement model benefitting all children and the therapeutic care provided;
- Medical staff monitoring every 90 days of the written prescription from a physician that recommends services. Unlike schools this requirement guarantees that current medical standards of professional practices for monitoring and assessing care are appropriate and available for billing by the State;
- Regularly scheduled reviews of all therapies are required, complaints, and concerns regarding child development and health improvement are medically reviewed' and
- Review of the findings, conclusions, recommendations and actions taken as part of quality review to ensure accurate and appropriate services to all children deemed medically necessary and through the IEP process.

The attached spreadsheets exemplify the point. There are a number of costs which programs other than Just Kids appropriately allocate to their education program cost centers. The approximate total of these costs which are borne by the D & T Clinic, although otherwise legitimate educational costs, is $1.4M (or $4.2M for the three year audit of Just Kids Learning Center). These costs can be categorized as Supervisor/Director Salaries and Facility Costs. The attached chart reflects 7 titled positions whose full salaries are paid exclusively by the D & T Clinic, except for the Executive Director who reports less than a full FTE in the School cost center. An additional chart reflects certain facility costs which are borne exclusively by the D & T Clinic although legitimate educational facility costs. (See: Facility Cost). The inclusion of these costs into our school tuition would increase our tuition by that same amount. (See: Analysis of Salaries/Business Office/Facility Costs).

While we believe the validity of NYSED's analysis and review is in itself sufficiently compelling to set aside the auditors' narrative on cost-effectiveness, we also challenge particular aspects of the auditors' analysis beyond the mere failure to conduct the appropriate comparisons. We understand that the auditors identified salary costs reported by "similar providers" on the CFR and simply divided that amount by the number of reported FTEs. As conceded in their response to specific questions concerning their analysis, the auditors clearly failed to consider the data reported by the SED-4 - - supplemental data which speaks directly to productivity and staff efficiency which are essential factors of consideration in determining whether a transaction is cost-effective. Additionally, the sample of 8 CFR #4a reports from which the auditors concede to have obtained salary information upon which they derived "hourly rate" data reports salary only, does not report associated fringe and is an exceedingly under-represented sample.

The auditors' response to specific challenges to their analysis confirms our understanding that the auditors, by design, did not reflect the cost of supervision which is included within the calculation of the Clinic charge. This failure supports our challenge that the comparison of the Clinic charge to "similar program" stand-alone therapist charges is inaccurate.

Auditors further concede that there was no review of the terms or conditions of the stand-alone therapists' engagement by the "similar programs" to determine whether supervision was provided. By auditors own admission "the analysis was based solely on reported data" which Just Kids asserts was incomplete.

Auditors also concede to having failed to consider whether the cost of the contracted therapist also included the facility costs associated with the space utilized by the "similar program" as is the case with the D & T Clinic charge. The auditors' analysis unduly limited consideration of costs associated with the clinician to salary alone, ignoring costs associated with supervision and facility utilization.

The auditors' further assertion that "other similar" providers' costs are substantially lower than the rates charged by Just Kids is simply factually inaccurate. Based upon that calculation, each of the "other" providers would be charging a rate for clinical services well below the County's own "related service only" rate of reimbursement - - an obviously unlikely possibility.

These seemingly minor errors ultimately skew the data upon which the auditors base their finding. Moreover, as the attached documentation attests, the auditor's designation of "similar providers" appears to ignore significant sectors of the market including school districts and other entities in determining the "market value" of the services. Clearly, several entities purchased services from the D & T Clinic at a rate <u>greater</u> than the fee charged to the School. It does not appear that these market forces were included in the auditors' analysis - - an oversight which we believe skews the result.

Moreover, as auditors concede, there was great variation in the type of program selected by the auditors as "similar", the commonality limited to approval as a 4410 program. Again, we assert that the singularly appropriate comparison would be with other article 28 clinics which also operate 4410 programs. Any other comparison weakens the validity of the result.

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While any one of the weaknesses in the auditors' analysis identified above would be reason enough to set aside the auditors' narrative, the totality of the weaknesses - - including the misapplication of "comparability data" and the challenge to the Department's own well-reasoned analysis - - when taken together compel reassessment of the auditors' position that the narrative is either appropriate, warranted or valid.

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Comment
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Just Kids has an impeccable reputation of delivering quality and innovative services to children with special needs on Long Island. This is a testament to the dedication of the nearly 500 staff that work for Just Kids and the D & T Clinic. Through the years, Just Kids has been very open with its communication with SED and this carried through to the OSC audit. Furthermore, Just Kids continues to be a low cost provider of special education services on Long Island, with tuition rates approximately 12% below the regional average.

Accordingly, we respectfully, but vehemently, request the narrative be deleted from the Report.

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We appreciate the courtesy and professionalism extended to Just Kids in the course of the audit and respectfully request reconsideration of the items highlighted above.

Very truly yours,

GREENBERG TRAURIG, LLP

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Enclosures
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State Comptroller's Comments

1. We revised our report to delete the recommended disallowance for non-allowable food expenses. In addition, we reduced the disallowances for repairs and maintenance (including grounds-keeping services) and office supplies by $7,631 and $5,043, respectively, and revised the report as appropriate.
2. It is not reasonable to compare the day care discount to "related party transactions" and health insurance coverage. Generally, a grandchild is not covered under a grandparent's health insurance plan, unless the grandchild is a dependent. Just Kids officials provided no evidence that the grandchildren were dependents of the day care discount recipients.
3. Just Kids officials advised that the intent of the discounted day care fees was to retain employees and attract students to its Integrated Program. However, the 17 individuals in question were not parents of the children in Just Kids programs; they were grandparents, an aunt, and in one case an individual who did not work for Just Kids. There is no evidence that the grandparents, aunt, or any other employee would have ended employment with Just Kids if they did not receive the day care discount. Further, since the day care program included infants, the intent of this discount was not just for the growth of the school's Integrated Program.
4. In May 2015, Just Kids' Executive Director informed us that time records were not required for this employee. Further, the invoices, photographs, and other documents provided to the auditors were insufficient to support the work performed by this employee.
5. According to the employee's employment contracts, the assigned tasks were required to be performed during the late afternoons, and not on an "as needed" basis or by the agency's next day of operation. The site visits were conducted during the time periods specified in the employee's contracts. The employee could not be located during those visits.
6. The notion that the employee worked "primarily at the beginning and end of the school year" was not a suggestion made by the auditors; rather, it was a statement by Just Kids' Executive Director.
7. The letters addressed to the three administrative/executive level employees who received awards clearly state that the awards were merit-based and were non-recurring and non-accumulating, thus meeting the Manual's definition of a bonus. However, these employees were not in Direct Care titles, and therefore (per the Manual), they were ineligible for bonuses.
8. In their response, Just Kids officials acknowledged that two individuals were employed under Code 603. According to the CFR Manual, Code 603 employees are responsible for the overall fiscal management of the agency.
9. The auditors did not miscalculate the number of fiscal staff. They reported the actual number of employees rather than their full-time equivalents (FTEs). The nine employees mentioned on page 9 of the report equate to approximately five FTEs as noted in Just Kids' response. We have revised our report to make it clear that the nine employees equated to approximately five FTEs.
10. We maintain that Just Kids fiscal staff should have possessed the necessary technical skills to perform the tasks for which the consultant was hired.

11. We did not mischaracterize the services of the agency's CPA firm. Rather, we were clear about the CPA's role. As stated on page 9 of our report, the internal control assessments and testing done during the CPA's certification of the financial statements and CFR should have provided reasonable assurance of Just Kids' internal controls and financial integrity.
12. See Comment no. 10.
13. According to the Manual, cell phone charges that are not properly documented will not be reimbursed. While we understand the program's need to have phone contact with the employee, Just Kids and/or the employee failed to sufficiently document the cell phone charges.
14. We acknowledge that the frequency of staff meetings is a programmatic decision. Nevertheless, it is not necessary nor cost-efficient for an employee to make duplicate trips to the same location on a daily basis. As evidenced by the AED's timesheet and travel vouchers, she spent about 30 minutes at the Middle Island location each morning only to travel to a field site where she worked a portion of the day and then traveled back to the Middle Island location, where she spent about an hour before ending her day. We do not question that the face-to-face meetings were at the insistence of the Executive Director. Nonetheless, we maintain that the routine travel to and from the Lindenhurst and Middle Island sites was unnecessary and unreasonable, and it could have avoided with better planning.
15. The State Comptroller's authority to audit the costs submitted by Just Kids on its CFRs to SED is expressly cited on pages 3 and 12 of the report. OSC has the legal authority to make recommendations to SED that, in this case, may impact Just Kids payments. Our authority was also stated in the copy of the engagement letter that was sent to Just Kids.
16. Our review is independent of SED. We have a responsibility to report our findings as legally authorized and required, and in accordance with Generally Accepted Government Auditing Standards. Our recommendations are not a substitute for SED's judgment. We acknowledged SED's prior approval of the transactions. Thus, the expenses in question were not recommended for disallowance, but rather to be reviewed within the context of our audit findings.
17. See Comment no. 16.
18. Just Kids assertion is incorrect. OSC acknowledged SED's approval of the transactions. Our review of the claimed expenses falls within the audit protocols of determining whether the costs are allowable.
19. OSC has legal authority to report on the matters identified.
20. We maintain that our summary and description of the arrangements are accurate.
21. We did not disregard SED's approval of the lease. However, we maintain that SED should re-evaluate any new lease arrangements because certain provisions of the current lease are inconsistent with the Manual's prescriptions pertaining to less-than-arm's-length lease transactions – in particular, the Manual's requirement that reimbursement be based on the owner's actual cost or fair market value, whichever is less.
22. We maintain that upon expiration of the existing lease, SED could determine that the basis for further approval, including extension of the allowance provisions in question, is no longer valid.
23. We question the extent to which SED Counsel is "constrained to recognize the lease as a matter of law." As noted in our report, the Manual (which SED publishes pursuant to

its statutory and regulatory authority) authorizes SED to withhold approval of a less-than-arm's-length transaction (such as the lease with Cam-Held Enterprises) based on a fair presentation of all relevant facts, data, or issues and the adequacy of supporting documentation. As such, SED likely has considerable latitude with respect to its review and approval of any lease renewal agreement between Just Kids and Cam-Held Enterprises.

24. The fact remains that, pursuant to the Manual, the lower of an owner's actual costs or fair market value is the amount that is reimbursable in a less-than-arm's-length lease transaction. Moreover, consistent with the Manual, Just Kids should not be compensated for costs it did not incur when the property's market value exceeds Just Kids' actual costs to maintain and operate it.
25. Just Kid's assertion is speculative. Further, because the Diagnostic & Treatment Center (D & T) can provide services to other clients (besides Just Kids), Just Kids should not be responsible for 100 percent of D & T's leasehold costs, and therefore it is appropriate for D & T to assume some portion of such costs.
26. We acknowledge that there could have been certain limitations in our analysis of Contracted Therapeutic Services. Nevertheless, the fact remains that the hourly rates charged by D & T (and paid by Just Kids) were often higher than the rates charged by other providers of the same therapies in Suffolk County. Further, related service providers (whether it's D & T or any other provider) commonly incur operating costs other than the direct costs of the therapists themselves - and such other costs are generally included in the rates charged by the providers. Consequently, without a detailed analysis, it is quite unclear that the various cost components referenced by Just Kids reliably illustrate the comparable cost advantage of Just Kids' arrangement with D & T. As such, we maintain that SED should re-evaluate this matter.
27. We acknowledge that SED performs an analysis of Just Kids' costs annually. Nevertheless, based on our audit fieldwork and analysis, we continue to question whether the arrangement between Just Kids and D & T remains appropriate. Therefore, we recommended that SED review the propriety of the D & T arrangement, and SED agreed to do so.