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
East River Child Development Center

Report 2016-S-3

July 2017

Executive Summary

Purpose

To determine whether the costs reported by the East River Child Development Center (ERCDC) on its Consolidated Fiscal Report (CFR) were reasonable, necessary, directly related to the special education program, and sufficiently documented, pursuant to the State Education Department's (SED) guidelines, including the Reimbursable Cost Manual (Manual). Our audit covered the fiscal year ended June 30, 2014.

Background

ERCDC is a New York City-based not-for-profit organization authorized by SED to provide Special Education Itinerant Teacher (SEIT) and full-day Special Class (SC) preschool special education services to children with disabilities who are three to four years of age. For purposes of this report, these programs are collectively referred to as the SED cost-based programs. During the 2013-14 school year, ERCDC served about 96 students in its center-based SC program. ERCDC is reimbursed for preschool special education services through rates established by SED. The reimbursement rates are based on the financial information that ERCDC reports to SED on its annual CFRs. To be eligible for reimbursement, reported costs must comply with the Manual requirements and be reasonable, necessary, directly related to the special education program, and sufficiently documented. For the fiscal year ended June 30, 2014, ERCDC reported approximately $4.9 million in reimbursable costs for the audited cost-based programs.

In addition to the cost-based preschool special education programs, ERCDC operates two other SED programs: Evaluations and 1:1 Aides. However, payments for services under these other programs are based on fixed fees, as opposed to the cost-based rates established through CFR-reported financial information. ERCDC also receives monetary grants from other governmental and private sources.

Key Findings

For the fiscal year ended June 30, 2014, we identified $350,246 in ineligible costs that ERCDC reported on its CFR and recommend such costs be disallowed. These ineligible costs included $340,064 in personal service costs and $10,182 in other than personal service costs. Among the ineligible costs identified were:

- $116,508 in retirement plan payments for certain ERCDC employees that were not proportionally similar to benefits for general ERCDC staff;
- $89,940 in compensation costs for ERCDC's Comptroller, who did not perform many of the functions normally required of that position;
- $52,266 in employee compensation that was not properly supported by time and attendance records; and
- $43,025 in salaries and fringe benefits paid to 1:1 aides that were charged to the SC preschool special education program, but should have been charged to the 1:1 Aides program.

Key Recommendations

To SED:

- Review the recommended disallowances resulting from our audit and make the appropriate adjustments to the costs reported on ERCDC's CFR and tuition reimbursement rates.
- Work with ERCDC officials to help ensure their compliance with the provisions in the Manual.

To ERCDC:

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

Other Related Audits/Reports of Interest

Aim High Children's Services: Compliance With the Reimbursable Cost Manual (2015-S-62)
Hebrew Institute for the Deaf and Exceptional Children: Compliance With the Reimbursable Cost Manual (2015-S-67)

State of New York
Office of the State Comptroller

Division of State Government Accountability

July 21, 2017

Ms. MaryEllen Elia
Commissioner
State Education Department
State Education Building – Room 125
89 Washington Avenue
Albany, NY 12234

Mr. Brian Zimmerman
Executive Director
East River Child Development Center
577 Grand Street
New York, NY 10002

Dear Ms. Elia and Mr. Zimmerman:

The Office of the State Comptroller is committed to helping State agencies, public authorities, and local government agencies manage their resources efficiently and effectively. By so doing, it provides 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. 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 expenses submitted by East River Child Development Center to the State Education Department for the purposes of establishing 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

East River Child Development Center (ERCDC) is a New York City-based not-for-profit organization authorized by the State Education Department (SED) to operate Special Education Itinerant Teacher (SEIT) and full-day Special Class (SC) preschool special education services to children with disabilities who are three to four years of age. For purposes of this report, these programs are collectively referred to as the SED cost-based programs. ERCDC has an Executive Director (ED), who is responsible for the overall general administration of ERCDC. The ED is appointed by, and under the general direction of, the governing board of the agency.

ERCDC offers an array of special needs services including: specialized instruction, speech therapy, occupational therapy, physical therapy, counseling, assistive technology, and parent education. ERCDC delivers its services in its center-based preschool classes, special education itinerant services in home, day care, or Head Start settings. ERCDC employs bilingual therapists servicing clients who may need assistance in languages other than English. Currently, these include Chinese (Mandarin) and Spanish.

The New York City Department of Education (DoE) refers preschool students to ERCDC based on clinical evaluations and pays for ERCDC's services using rates established by SED. The State, in turn, reimburses the DoE 59.5 percent of the reimbursement rates it pays to ERCDC. These rates are based on the financial information that ERCDC reports to SED on its annual Consolidated Fiscal Reports (CFRs). To qualify for reimbursement, costs reported on the CFR must comply with the criteria set forth in SED's Reimbursable Cost Manual (Manual). In addition, ERCDC must meet the reporting requirements prescribed in the Consolidated Fiscal Reporting and Claiming Manual (Claiming Manual). Reimbursable costs must be reasonable, necessary, and directly related and have adequate substantiating documentation.

Section 4410-c of the Education Law requires the State Comptroller to audit the expenses reported to SED by special education service providers for preschool children with disabilities. For the fiscal year ended June 30, 2014, ERCDC reported approximately $4.9 million in reimbursable costs for the audited cost-based programs.

In addition to the SEIT and SC cost-based preschool special education programs, ERCDC also operates two other SED programs: Evaluations and 1:1 Aides. However, reimbursement for services under these other programs are based on fixed fees, as opposed to the cost-based rates. ERCDC also receives monetary grants from other governmental and private sources.

Audit Findings and Recommendations

For the fiscal year ended June 30, 2014, we identified $350,246 in reported costs that did not comply with the Manual's requirements for reimbursement. The ineligible costs included $340,064 in personal service costs and $10,182 in other than personal service (OTPS) costs (see Exhibit at the end of the report).

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 CFR as either direct care costs (e.g., teachers' salaries) or non-direct care costs (e.g., administrators' salaries). All claimed costs must comply with the applicable provisions of the Manual. For the fiscal year ended June 30, 2014, ERCDC reported $4,335,883 in reimbursable personal service costs. We identified $340,064 that did not comply with the Manual's guidelines for reimbursement, detailed as follows:

Distributions to Employee Retirement Accounts

According to the Manual, "Benefits including pensions … for individual employees or officers/directors are proportionately similar to those received by other classes or groups of employees."

ERCDC paid $116,508 to the third-party administrator who managed a 401(k) program, as a distribution on behalf of certain employees as follows:

- $76,971 for 28 employees who were previously part of the 401(k) program and opted to transition to the 403(b) and made contributions into it in 2014;
- $32,569 for 15 employees who participated in the 401(k) program but did not transition to or participate in the 403(b) and, consequently, made no contributions; and
- $6,968 for two additional employees who were not part of either the 401(k) program or the 403(b) program.

Additionally, there were two employees who participated in both plans but did not receive any amounts of the distribution.

The distributions were made on behalf of 43 (of the 66) ERCDC employees who participated in the pension plans. Two employees who did not participate in any plan received a distribution. The distributions ranged from a high of 5.5 percent to as low as zero. On September 1, 2016, the ED advised us that distributions were also based on an employee's evaluation or his discretion. We requested 17 evaluations, but we received 11 (four with "excellent" ratings, four with "very good" ratings, two with "good" ratings, and one with a rating of "exceeds expectations"). Five of the 11 employees with evaluations received a distribution, but the other six did not. Also, although the 11 employees received "good" to "excellent" ratings on their evaluations, not all of them received distributions equal to the distributions for executive management. Thus, it was unclear whether the contributions corresponded with performance evaluation ratings. Of the remaining six evaluations, five were for staff who were no longer employed by ERCDC, and one was for a SEIT. We concluded that the distributions were not proportionately similar for all staff, as required by the Manual. Therefore, we recommend SED disallow the $116,508 distribution.

In response to our preliminary findings, ERCDC provided several documents, including: descriptions of the 401(k) and 403(b) programs; the transition from one program to the other; distributions made to employees for fiscal years 2013 and 2014; actuarial tests; IRS "Top Heavy" test results; and an Incentive Savings Trust Amendment. In addition, ERCDC indicated we should not use the terms "401(k) contributions and or distributions into the employees' 401(k)," but rather "The Plan." However, we did not change our report because it accurately reflects how these transactions were referenced in the documents reviewed during the audit.

Moreover, after reviewing these documents, we concluded that the amounts in question should still be disallowed because the distributions were not made equitably to staff. None of the aforementioned documents addressed the basis for the disallowance, but rather described certain attributes of the overall plan, which we did not challenge. The documents were not relevant to the basis for the amount of the recommended disallowance.

Health Care Coverage – Eligibility and Reimbursement

The Manual specifies that benefits for individual employees or officers/directors be proportionately similar to those received by other classes or groups of employees. The Manual also requires that expenses be sufficiently documented.

We reviewed the personnel files of 33 sampled employees to determine whether they met ERCDC's health care eligibility criteria. From a review of the payroll registers, we determined that the ED and the Comptroller were reimbursed $35,712 in health care costs for fiscal year 2013-14 (including $32,163 for health care and $3,549 for dental care). Part of the reimbursement represents expenses incurred for insurance and out-of-pocket payments. The amount was added to their payroll checks as a reimbursement; however, there were no records (e.g., invoices, vouchers, checks) at ERCDC to support these payments. Further, such reimbursements are not addressed by ERCDC policy (handbook) and are not afforded to any other employees.

ERCDC's practice is for employees to contribute toward their health care coverage. However, we noted two other employees who did not contribute toward their health care benefits during fiscal year 2013-14. We made inquiries to ERCDC's Comptroller, who responded that this accommodation was made for these two employees because they were part of ERCDC's management. Also, according to ERCDC's ED, because the two employees were considered management, they were exempt from contributing toward health care benefits. The ED stated that this practice is supported by the Manual (Section II.13.B: Fringe Benefits). However, the Manual also requires benefits to be proportionately similar for all employees for whom costs are claimed for reimbursement.

As a result, we recommend SED disallow $36,317 in health care benefits ERCDC paid that were not proportionately similar for all employees.

In response to the preliminary finding, ERCDC officials reiterated that it is their prerogative to establish different classes of employees for determining health care benefits, including ERCDC's funding of such benefits. However, ERCDC did not have written policies permitting this practice. In addition, ERCDC gave us a copy of their employment contract for fiscal year 2015-16 and the minutes from December 2014 and 2015 meetings of the Board of Directors. However, the employment contracts did not cover the fiscal year (2013-14) audited. Moreover, even if ERCDC formally approved this practice, the related costs should not have been claimed for reimbursement because the benefits in question were not afforded to all employees.

Time and Attendance

According to the Manual, compensation costs must be based on approved, documented payrolls, 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. For the fiscal year ended June 30, 2014, we reviewed time and attendance records, EasyTrac notes, and personnel files for 33 employees whose salaries totaled $1,595,627. Of the 33 employees, we determined that 27 did not have sufficient documentation to support $52,266 in claimed compensation costs. For example, we determined that:

- Several employees signed in at the beginning of certain workdays, but they did not sign out at the end of the days in question. The employees were paid $30,074 for these days, although there was insufficient documentation to support they actually worked full days.
- 19 employees departed 30 minutes early because they did not take a lunch break and were paid $6,519; however, they were not eligible for a paid lunch.
- 6 employees exceeded the 10 days allowed for leave and were paid $5,349 for those days.

Therefore, we recommend SED disallow $52,266 in salary due to a lack of supporting documentation.

Comptroller's Title and Responsibilities

According to the Claiming Manual, Appendix R: "Comptroller (position title 603) is responsible for overall fiscal management of the agency. Also, includes Business Official, Director of Finance." In addition, ERCDC's Comptroller's job description lists 12 significant responsibilities.

The Manual (Section II.13.A.(5)) states, "Compensation to all individuals who have a financial interest in the program including shareholders, trustees, board members, officers, family members or others and who are also program employees must be commensurate to actual services provided as appropriately qualified program employees or consultants and shall not include any distribution of earnings in excess of reimbursable compensation. Compensation shall not exceed the average regional levels paid by similar private providers to comparably qualified and appropriately certified personnel for similar work and hours of employment."

On March 30, 2016 and July 11, 2016, we met with the Comptroller to obtain an understanding of her duties and responsibilities and how they are carried out on a day-to-day basis. The Comptroller stated that the daily duties include accounting and payroll. She added that, on a daily basis, sessions of speech therapy, occupational therapy, physical therapy, and counseling are recorded on a spreadsheet. The Comptroller also stated that the purpose of the monthly attendance review is to ensure that the children are receiving the appropriate amount of therapy sessions prescribed by their Individualized Education Plans (IEPs).

Further, the Comptroller maintains the Certified Monthly Roster (CMR), which is the database the DoE uses to track payments. Once children are certified at the end of the month (whether for SEIT or center-based payments), the Comptroller checks the CMR on the NYC payee portal to follow the payment from the DoE. She showed us an example of a pending tuition payment.

The Comptroller also reviews invoices from vendors for payment processing and performs monthly bank reconciliations. However, the Comptroller is not responsible for ERCDC’s profit and loss statements. The profit and loss statement is prepared by the ED, who is responsible for other financial management functions usually overseen by the Comptroller. For example, the ED handles ERCDC’s trial balance, balance sheet, and statement of activities. Financial positions and functional expenses are handled by the ED. Furthermore, according to the Comptroller, the ED shares the responsibility for cash flow analysis as well as the handling of accounts receivable and accounts payable.

The job description states that the Comptroller serves as the liaison between ERCDC and various State and City agencies, trade groups, and business partners, and assists in improving and maintaining internal operating procedures; the ED (and not the Comptroller) completes and maintains budget projections for management and Board members. At a meeting with the Comptroller, we requested documents to support the tasks that were accomplished for a sample of 24 days during the school year. Our review of the documents indicated that the primary functions were payroll review, accounts payable, and CMR maintenance. In addition, the Comptroller showed auditors how to access a software application through a computer portal. The Comptroller did not provide any other relevant documentary evidence of her activities beyond the tasks previously detailed.

Based on the available evidence, we concluded that ERCDC’s Comptroller performed about 42 percent of the tasks listed for the position of Comptroller, and therefore, did not fulfill most of the duties associated with that position. Consequently, the Comptroller’s salary ($163,692) was not commensurate with the duties she actually performed. We reviewed the Claiming Manual Appendix R to select the title most appropriate given the tasks that were performed and concluded that the appropriate position/title for this employee was code 606 - Accountant (Agency Administration). The responsibilities for this position are stated as: “responsible for the establishment and maintenance of the agency’s systematic fiscal transactions and preparation of financial statements for the agency.”

For position 606 Accountant, SED provided a median salary of $68,213 for the region where ERCDC is located. However, ERCDC claimed $163,692 for the Comptroller (or $95,479 more than the median salary limitation). Consequently, we recommend that SED disallow $89,940 (the portion of the $95,479 allocated to the SED cost-based programs).

Allocation of Staff's Time Between Programs

The Manual requires costs be allocated on a reasonable basis, either based on time study or other documented basis such as square footage. However, we identified three instances wherein ERCDC could not document a reasonable basis for the allocations of certain costs on the CFR.

Allocation of 1:1 Employees

A portion of the personal service costs of ERCDC's 1:1 aides were allocated to the SC program. The ED advised that it was his understanding this was acceptable under the Manual. He added that the 1:1 Aides program is funded at a daily rate for each school day the child is enrolled. However, since 1:1 aides are separately funded from the SC program, all costs associated with the provision of 1:1 aide services should be reported under the 1:1 Aides program. Moreover, ERCDC staff are paid 260 days even though the school is open only 210 days. As a result, funding is not being provided for 50 days that full-time, year-round 1:1 aide staff are paid for. Also, the ED indicated that some of his 1:1 aides have long-term experience in 1:1 support. Consequently, when a 1:1 student is out, the related aide can still be in the classroom or be redeployed to support other needs (e.g., substitute aide, administrative work).

ERCDC's daily rate for 1:1 aides is $119.97. The school year includes 180 days for the regular school year and 30 days for the summer term – or a total of 210 days for a full year. As such, the total annual charge for an aide should have been $25,194 ($119.97 × 210). However, ERCDC incurred costs above this amount for one part-time and four full-time 1:1 aides and charged the excess costs to the SC program. There was no basis for charging the excess costs of the four full-time aides and part of the part-timer's costs to the SC program. This was also contrary to the pertinent provisions of the Claiming Manual.

Specifically, the Claiming Manual's general instruction, Section 8.0, requires that "expenses and revenues and FTE enrollment for approved 1:1 teacher aides (preschool and school age) must be reported as a separate column (Program Code 9230). Salary and fringes of the 1:1 aide(s) and ratio value allocation of agency administrative costs are the only expenditures required to be reported in this program code." The Manual also states that "all 1:1 aide costs (salaries, fringe benefits of the aide and allocated direct and indirect costs) should be reported in one separate cost center on the providers' financial reports." Table 1 summarizes the excess costs charged to the SC program for the 1:1 aides.

Table 1

Employee	Total Salary Costs Claimed	1:1 Allowed at the Daily Rate	Excess Charged to the Preschool Special Education
A	$32,123.10	$25,194	$6,929.10
B	27,973.02	25,194	2,779.02
C	3,721.43	3,599	122.43
D	35,049.90	25,194	9,855.90
E	28,769.13	25,194	3,575.13
Totals	**$127,636.58**	**$104,375**	**$23,261.58**

For the fiscal year ended June 30, 2014, ERCDC paid 13 aides a total of $298,288. Of this amount, $185,650 was allocated to the 1:1 program by ERCDC on its CFR, with the balance ($112,638) charged to the SC program. However, as detailed in Table 1, we determined that $23,262 should be reallocated from the SC program and charged to the 1:1 Aides program. Accordingly, we recommend SED disallow $23,262 in teacher aide salary from the SC program.

Also, ERCDC incurred $19,763 in fringe benefit costs for the 1:1 Aides program, which it transferred from the 1:1 Aides program to the SC program on the CFR. This was contrary to the Manual's requirements; and therefore, we recommend that the $19,763 in fringe benefit costs be disallowed from the SC program as well.

Housekeeping and Maintenance Costs

ERCDC did not allocate housekeeping and maintenance personal services charges among its various programs, as otherwise required by the Manual. All housekeeping and maintenance staff costs were charged to the SC program, although housekeeping and maintenance services were required for areas used for SEIT and agency administration activities. According to the ED, an SED accountant told them not to allocate these costs. However, there was no documentation of such purported SED guidance. Moreover, providers such as ERCDC must consistently comply with the applicable provisions of the Manual.

Appendix I of the Claiming Manual states:

> *Service Providers should note that* **all attempts should be made to directly charge an expense** *to the appropriate cost center (agency administration or program/site and program administration). If you are unable to direct charge expenses to agency administration or program/site(s) and program administration, the following includes [an example] of recommended allocation methods:*

Expense Item	Recommended Allocation Method
Repairs and Maintenance and Janitorial and Housekeeping Staff	Square Footage

For fiscal year 2013-14, ERCDC reported Housekeeping and Maintenance salaries of $109,820. However, these salary costs were not allocated among the appropriate programs. Allocation of the salaries, based upon square footage, resulted in a reduction of $13,204 to the Housekeeping and Maintenance salaries charged to the SC program. The reallocation of the Housekeeping and Maintenance salaries (without the allocation of administration costs to program areas) is summarized in Table 2.

Table 2

Programs	Amount Claimed	Amount Allocated Per Audit	Difference
SEIT	$0	$9,221.50	$9,221.50
Evaluations	$0	$1,886.22	$1,886.22
Agency Admin	$0	$2,095.80	$2,095.80
Preschool SC	$109,819.68	$96,616.17	($13,203.51)

Based on our analysis, we recommend SED disallow Housekeeping and Maintenance personal service costs totaling $2,008. The disallowance includes $1,886 for Evaluations and $122 (or $2,096 × .058) for agency administration costs.

Allocation of SEIT Personal Service Costs

One SEIT employee's salary was divided between the SEIT and the SC programs, while time sheets showed $4,060 of the employee's time was spent in the SEIT program. According to the ED, this was an error. In this instance, we do not recommend a disallowance. However, we recommend that $4,060 in personal service costs be reallocated from the SC program to the SEIT program.

Other Than Personal Service Costs

Consultants

To be reimbursed for consultant costs, the Manual requires adequate documentation that includes (but is not limited to) the consultant's résumé, a written contract that includes the nature of the services to be provided, the charge per day, and service dates. All payments must be supported by itemized invoices that indicate the specific services actually provided and, for each service, the date(s), number of hours provided, fee per hour, and total amount charged. In addition, when direct care services are provided, the documentation must indicate the names of students served, the actual dates of service, and the number of hours of service to each child on each date.

For fiscal year 2013-14, ERCDC paid a consultant, SPOTS, $57,235 for 880.54 hours. SPOTS provided 1,358 sessions of occupational therapy services. However, each session was 30 minutes, accounting for 679 hours of direct time valued at $44,135. The remaining 201.54 hours were not supported in the invoices used by ERCDC as its supporting documentation.

Occupational therapists enter their session notes into DoE's EasyTrac system after they provide therapy services. Following meetings with SED and ERCDC officials, we determined that five minutes per session was a reasonable amount of time to enter session notes into EasyTrac. However, when a child was absent, and therefore a scheduled therapy session did not occur, there was no need for five minutes to enter a session note. As noted previously, ERCDC paid SPOTS for 1,358 sessions in fiscal year 2013-14. Students were present for 1,146 occupational therapy sessions and absent for 212 (1,358 - 1,146) sessions. The allotment of five minutes per session when the student was present totals 95.5 hours, which when paid at a rate of $65 per hour totals $6,208. This reduced the unaccounted for occupational therapy time to 106.04 hours (201.54 - 95.5), or $6,893.

Additionally, the standard school day ran from 8:30 a.m. to 1:30 p.m., for a total of five hours, resulting in a maximum of ten half-hour sessions that a single therapist could provide per day. However, we found 14 days where therapists recorded more than ten sessions per day individually. We recommend SED disallow $585 in occupational therapy costs for the 18 sessions in excess of the maximum possible amount of ten per day. We also found six instances where children received more sessions than their IEP required. The total cost of these sessions was $195.

The total recommended disallowance for occupational therapy contract services is $7,673 ($6,893 + $585 + $195).

Other Items

To be eligible for reimbursement, reported costs must comply with the Manual's requirements and be reasonable, necessary, directly related to the special education program, and sufficiently documented. Costs will not be reimbursable without appropriate written documentation. Further, all personal expenses are not reimbursable unless specified otherwise in the Manual. Gifts of any kind and the costs of food provided to any staff are non-reimbursable.

However, we found $2,509 (of this amount $685 is direct care and $1,824 is agency administration) in various other OTPS expenses reported for fiscal year 2013-14 that were not in compliance with the Manual. Details of four ineligible costs, totaling $2,195, are presented as follows:

- $417 for the bulk purchases of groceries, with no evidence that they were used for the children. Furthermore, ERCDC's program is not authorized for a lunch component.
- $1,510 in insufficiently documented expenses related to a commercial litigation and business law practice. The invoice did not provide a detailed description of the services rendered.
- $90 in credit card purchases for coffee and for a holiday gift package, which are ineligible expenses.
- $178 in insufficiently documented credit card charges, including those for travel, food, and snacks. We were not provided with any supporting documentation for the travel expense. In regards to the food and snacks expense, the memo in the 2014 general ledger indicates that this expense was for snacks for classes one through seven; however, the

receipt listed a sale of $92.54 and an additional $20 for a tip, without specifying what was actually purchased. We visited the website for the vendor and found it was a bar and grill.

In addition, ERCDC is a 501(c)(3) not-for-profit organization and thus is sales tax exempt under State law. According to the Department of Tax and Finance, an educational organization (such as ERCDC) must file a form ST119.2 application to obtain tax-exempt status. However, of the 50 OTPS transactions selected for review, 12 transactions included sales taxes totaling $314. According to the ED, ERCDC had not submitted the ST119.2 tax-exempt application at the time the transactions in question were made, and consequently, ERCDC paid sales taxes on them. Subsequently, ERCDC submitted an ST119.2, and as of October 2013, ERCDC no longer pays sales taxes. Therefore, we recommend that SED disallow $314 because the sales tax was not a necessary expense.

Thus, we recommend that SED disallow $2,509 ($2,195 + $314) for these ineligible costs. (Note: SED had already made certain other adjustments to OTPS costs reported on the CFR.)

Other Matter

As stated in the Manual (Section III.1.C.(3)), "Requests for proposals (RFP) or other bidding documentation must be kept on file by the entities operating the program. The entity will need to justify that the consultant hired was the most economical and/or appropriate available for a particular service." As noted previously, ERCDC paid SPOTS $57,235 during the 2013-14 fiscal year. The ED advised us that they entered into the SPOTS contract because one of the occupational therapists employed by ERCDC owns a firm that provides occupational therapy services, and according to the ED, the rate of $65 per hour was a good rate. He added that the DoE pays $90 per hour. Furthermore, according to the ED, consultants from SPOTS are paid for direct time, per session as opposed to per hour, and they are not paid for non-direct services (e.g., logging session notes, travel or communication with a child's guardian). However, the ED did not have documentation to justify that the consultant hired was the most economical and/or appropriate available for a particular service. Consequently, there is less assurance that the occupational therapy services were obtained at the best price.

Recommendations

To SED:

1. Review the recommended disallowances resulting from our audit and make the appropriate adjustments to the costs reported on ERCDC's CFRs and tuition reimbursement rates.

2. Work with ERCDC officials to help ensure their compliance with the provisions in the Manual.

To ERCDC:

3. Ensure that costs reported on future CFRs comply with the requirements in the Manual.

4. Adjust the Comptroller's title to Accountant (position title 606), with a commensurate modification of salary, to reflect the tasks performed.

Audit Scope, Objective, and Methodology

The objective of this audit was to determine whether the costs reported by ERCDC on its CFR were reasonable, necessary, directly related to the special education program, and sufficiently documented, pursuant to the Manual. The audit included all expenses claimed on ERCDC's CFR for the fiscal year ended June 30, 2014.

To accomplish our objective, we reviewed the Manual, the Claiming Manual, ERCDC CFRs, and relevant financial records for the audit period. We also interviewed ERCDC officials and staff 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 related, and reimbursable. Specifically, we reviewed costs that were considered high risk and reimbursable in limited circumstances, such as consultants, non-mandatory fringe benefits, and time and attendance. Our sample was based on the relative materiality of the various categories of costs reported and their associated levels of risk. Our samples were not designed to be projected to the entire population of reported costs. Also, our review of ERCDC's internal controls focused on the controls over the 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 objective. We believe that the evidence obtained during our audit provides a reasonable basis for our findings and conclusions based on our audit objective.

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 Education Law.

Reporting Requirements

We provided draft copies of this report to SED and ERCDC officials for their review and formal comment. We considered officials' comments in preparing this final report and attached them to it. In their response, ERCDC officials generally disagreed with the report's findings, asserting that: auditors misinterpreted certain statements by ERCDC representatives during the audit; and there was misapplication of certain principles as set out in the Manual and as interpreted by SED officials. Nonetheless, in their response, SED officials agreed with our recommendations, and indicated they will continue to provide technical assistance when requested and that ERCDC should take advantage of CFR training available online on SED's website. Further, our rejoinders to certain ERCDC comments are included in the report's State Comptroller's Comments.

Additionally, with their response, ERCDC officials included about 140 pages of materials that were previously provided to and reviewed by OSC auditors during the course of the audit. We did not append these materials (some of which included confidential information) to this final report. However, the materials will be 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 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.

Contributors to This Report

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Division of State Government Accountability

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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

East River Child Development Center
Summary of Submitted and Disallowed Costs
for the 2013-14 Fiscal Year

Program Costs	Amount Per CFR	Amount Disallowed	Amount Remaining	Notes to Exhibit
Personal Services				
Direct Care	$3,913,049	$213,807	$3,699,242	A-C,F-I
Agency Administration	422,834	126,257	296,577	A,B,D,E
Total Personal Services	**$4,335,883**	**$340,064**	**$3,995,819**	
Other Than Personal Services				
Direct Care	$398,697	$8,358	$390,339	B,J,L
Agency Administration	150,585	1,824	148,761	B,I,J,K,M
Total Other Than Personal Services	**$549,282**	**$10,182**	**$539,100**	
Total Program Costs	**$4,885,165**	**$350,246**	**$4,534,919**	

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 ERCDC officials during the course of the audit.

A. Section II.13.B.(2).c – Cost for reimbursement of fringe benefit expenses shall be subject to the following principles: Benefits including pensions, life insurance and Tax Sheltered Annuities (TSAs) for individual employees or officers/directors are proportionately similar to those received by other classes or groups of employees.
B. Section II – Cost Principles, Introduction, "Generally, costs will be considered for reimbursement provided such costs are reasonable, necessary, directly related to the special education program and are sufficiently documented. Such reimbursable costs will be included in the calculation of tuition rates up to any limits or cost parameters approved annually in the rate setting methodology."
C. 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.
D. Section II.13.A.(4).d – For non-direct care staff under the 500 and 600 position title code series per Appendix R of the CFR Manual…compensation must be supported by time and effort reports or equivalent documentation.
E. Section II.13.A.(5) – Compensation to all individuals who have a financial interest in the program, such as family member, compensation should be commensurate to actual services provided as appropriately qualified program employees.
F. Section III.1.M.(1).(i) – Salaries of employees who perform tasks for more than one program and/or entity must be allocated among all programs and/or entities for which they work.
G. Section IV.2.F – All 1:1 aide costs (salaries, fringe benefits of the aide and allocated direct and indirect costs) should be reported in one separate cost center on the providers' financial reports.
H. Section III.1.M.(2) – Entities operating programs must use allocation methods that are fair and reasonable, as determined by the Commissioner's fiscal representatives. Such allocation methods, as well as the statistical basis used to calculate allocation percentages, must be documented and retained for each fiscal year for review upon audit for a minimum of seven (7) years. Allocation percentages should be reviewed on an annual basis and adjusted as necessary.
I. Section III.1.B – Actual hours of service are the preferred statistical basis upon which to allocate salaries and fringe benefits for shared staff who work on multiple programs. Entities must maintain appropriate documentation reflecting the hours used in this allocation. Acceptable documentation may include payroll records or time studies. If hours of service cannot be calculated or a time study cannot be completed, then alternative methods that are equitable and conform to generally accepted accounting principles may be utilized.

Documentation for all allocation methods (bases and percentages) must be retained for a minimum of seven years.

J. Section III.1.C.(2) – Adequate documentation includes, but is not limited to, the consultant's resume, a written contract which includes the nature of the services to be provided, the charge per day and service dates. All payments must be supported by itemized invoices which indicate the specific services actually provided; and for each service, the date(s), number of hours provided, the fee per hour; and the total amount charged.
K. Section III.1.C.(3) – Request for proposal (RFP) or other bidding documentation must be kept on file by the entities operating the program. The entity will need to justify that the consultant hired was the most economical and/or appropriate available for a particular service.
L. Section II.22.C – Costs of food provided to any staff including lunchroom monitors are not reimbursable.
M. Section II.24 – Gifts of any kind are not reimbursable.

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
O: 518.473-4706
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March 22, 2017

Ms. Carmen Maldonado
Audit Director
Division of State Government Accountability
59 Maiden Lane, 21st Floor
New York, NY 10038

Dear Ms. Maldonado:

The following is the New York State Education Department's (SED) response to the draft audit report, 2016-S-3, Compliance with the Reimbursable Cost Manual: East River Child Development Center (ERCDC).

In addition to the actions that will be taken in response to the specific recommendations described below, SED 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 ERCDC 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 the costs reported on ERCDC's CFRs and tuition reimbursement rates.

We agree with this recommendation. SED 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 ERCDC's officials to help ensure their compliance with the provisions in the Manual.

We agree with this recommendation. SED will continue to provide technical assistance whenever requested and will strongly recommend the ERCDC officials take advantage of our availability to help them better understand the standards for reimbursement as presented in

Regulation and the Reimbursable Cost Manual (RCM). Furthermore, Consolidated Fiscal Report (CFR) training is available online on SED's webpage. SED recommends that all individuals signing the CFR certification statements, namely Executive Directors and Certified Public Accountants, complete this training. At the direction of the Board of Regents, the Department intends to require that this training be mandatory and will require individuals to verify that they have completed the training.

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: Christopher Suriano
Belinda Johnson
Suzanne Bolling

Agency Comments - East River Child Development Center

East River
CHILD
DEVELOPMENT
CENTER
A NON-PROFIT EDUCATIONAL CORPORATION
577 GRAND STREET • NEW YORK, N.Y. 10002 • (212) 254-7300
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March 22, 2017

Ms. Carmen Maldonado
Audit Director
Office of the State Comptroller
Division of State Government Accountability
110 State Street, 11th Floor
Albany, N.Y. 12236

Re: Compliance with the Reimbursable Cost Manual
State Education Department
Draft report 2016-S-3

Dear Ms. Maldonado:

Management is obliged to the audit team for their efforts over the past year while auditing the expenditures of East River Child Development Center (ERCDC). We are pleased to have been able to provide documentation and explanations immediately upon request, and are confident that the auditors appreciated that respect and courtesy.

ERCDC management must, however, express a measure of disappointment at the auditors' findings given the nature and tenor of a good number of exchanges and communications between the audit team and representatives of ERCDC which reflected the audit team's assessment that ERCDC's records were "clean", even "impeccable", with "no contingent liabilities to be disclosed". While ERCDC communicated its availability to respond to any and all concerns or questions the audit team may have had, we are concerned that the auditors have not given appropriate weight to some of the explanations provided by the experts and consultants upon which management had relied.

ERCDC management reaffirms its challenge of OSC's audit findings and recommended disallowances in the preliminary reports and draft audit report as specified in each response provided by management and counsel for East River Child Development Center. ERCDC works tirelessly to assure that all of ERCDC's audited expenditures are reasonable, practical, considered sound business practice, and implemented with prudence given management's

* Comment 1

*See State Comptroller's Comments, page 35.

responsibility to the agency, SED and NYS tax payers; the expenditures reviewed in this audit year were no exception. Each of these expenditures were necessary, documented and directly related to and in furtherance of the education program and its administration.

East River Child Development Center serves children with special needs and their families throughout New York City in multidisciplined programs providing multicultural and multilingual educational and therapeutic services. ERCDC operates quality programs with integrity and transparency and has done so with exceptional reputation for nearly half a century.

As a result of a reduction in referrals for special education services together with the freeze on preschool special education tuition rates for 7 years, ERCDC has absorbed a reduction in revenues totaling $1.38 million between 2011 and 2015. However, through responsible and prudent financial management, ERCDC remains financially viable.

We have thus far been successful in keeping the structure of ERCDC intact while implementing cost saving measures without a reduction in services. We are concerned however, that ERCDC will face immediate and irreparable damage resulting from OSC's suggested disallowances and we implore the OSC to consider each of our presented challenges within that context.

Respectfully,

Brian Zimmerman
Executive Director

CC: Commissioner Elia, NYSED
Thalia Melendez, NYSED
Suzanne Bolling, NYSED
James Kampf, NYSED
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March 22, 2017

VIA ELECTRONIC EMAIL

Carmen Maldonado
Audit Director
Office of the State Controller
Division of State Government
Accountability
110 State Street, 11th Floor
Albany, New York 12236

RE: Compliance with the Reimbursable Cost Manual
State Education Department
East River Child Development Center
Draft Report 2016-S-3

Dear Ms. Maldonado:

We have reviewed the above referenced Draft Report and appreciate the opportunity to provide comment on the findings set out therein and the information presented in the several preliminary reports upon which the Draft Report is based, together with information presented during the exit conference. We renew the challenges advanced in the responses provided to the several preliminary reports, and respectfully request the Office's thoughtful consideration of these challenges. We believe that a select number of the presented findings are based upon errors in fact, misinterpretations of certain statements made by representatives of ERCDC during the audit process, and the misapplication of certain principles as set out in the Reimbursable Cost Manual and as interpreted by the New York State Education Department, as described in further detail below.

* Comment 1

Audit Findings and Recommendations

Personal Service Costs

Distributions to Employee Retirement Accounts

At the outset, we must correct certain misrepresentations ascribed to the Executive Director in the Report narrative which purports to describe the Agency's treatment of distributions to certain employee retirement accounts. As clarified during the exit conference, and the written response to the preliminary audit finding, management of ERCDC relied exclusively on the established competency of its retirement Plan Manager and the advice and direction of this financial attorney consultant. Management's

* Comment 2

participation in the distribution decision-making process was limited to providing the Manager with the payroll information of Agency employees – a census of all employees – who would then advise as to allowable amounts of distributions, compliant with IRS, ERISA, and Department of Labor testing standards for non-discrimination and proportionality. At no time did Agency management exercise any independent judgment beyond that provided by the Plan Manager, and at no time did Agency management deviate from the recommendations provided by that Manager.

We believe that the auditors misconstrued the Executive Director's discussion of employee performance evaluations as relevant to any decision or action relative to the amount of the distributions now challenged by the auditors. Consideration of employee performance evaluations, as management explained in great detail, related only to decisions around salary compensation, and was not a factor in the determination of employee retirement account distributions, as the auditors suggest.

We take particular exception to the auditors' assertion that none of the documents provided by the Plan Manager to the auditors "addressed the basis for the disallowance" or finding, when, in fact, the depth and comprehensiveness of these attestations, clarifying memos and explanations provided through legal documents to the auditors, clearly support our challenge that distribution decisions were made in complete reliance on the advice of the consultant, upon assurances of their propriety.

Accordingly, we renew our challenge to the auditors' finding that the distributions to employee retirement accounts failed to comply with the applicable provisions of the Reimbursable Cost Manual governing proportionality – that benefits including pensions for individual employees or officers/directors be proportionately similar to those received by other classes or groups of employees as initially presented in our response to the preliminary report.

As asserted in our response to the preliminary report, we believe the auditors have mischaracterized the percentage of "Safe Harbor" match in 2013. As reflected in the attached contribution listing prepared by the 401(k) Plan Managers, the correct percentage is 4% of gross earnings, not 5%. (See: Attachment A)

Moreover, as the document provides, a more appropriate and accurate description of the 401(k) contributions reflects a mandatory Safe Harbor contribution of $132,079.11 by ERCDC with employee deferrals of $230,319.17.

We would also clarify that ERCDC did not "switch" to a different retirement plan, but rather established a 403(b) plan effective 7/1/2013 which did not require a mandated Safe Harbor match. Amendment of the 401(k) plan terminated the plan's contribution provisions.

In addition, ERCDC did not "transition" from one plan to the other. Rather the existing plan, as stated above, was amended and a new alternative plan was established.

Moreover, the $116,508 distribution referenced by the auditors was not described in any context as an "employer-match", but rather was appropriately described as an employer discretionary contribution which, by definition, is distinguishable from the mandatory safe harbor "match".

Beyond these points of clarification, ERCDC challenges the auditors' conclusions that the 403(b) plan were inequitable or that any of the retirement plan costs failed to comply with the RCM requirements governing retirement funds. (See: Attachment B)

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As advised by ERCDC's retirement Plan Manager, each of the distributions made were fully compliant with IRS, ERISA, and Department of Labor testing standards for non-discrimination. As the attached correspondence from the Plan Managers reflects, discretionary contributions and deferrals were at all times compliant with applicable standards, and, therefore, the costs associated must be reinstated. (See: Attachment C)

Not only does the Plan Manager's provided documentation support elimination of this finding, but consistency with prior audit report determinations compels acknowledgement that "fringe benefits are proportionately similar where (as here) the benefits-to-salaries ratio is the same/similar among all employees". (See: OSC Report 2014-S-79, Page 6)

The facts, as presented here, unequivocally satisfy the test set out by the Office in previously released reports, thus compelling a reconsideration of the ERCDC Report finding.

Even were select amounts of distributions to be found disproportionate through some contortion of the applicable principles, only those identified "excessive" would be defensibly disallowable expenses, and not the totality of the distributions, as proposed here.

Health Care Coverage

At the outset, we must challenge the auditors' assertion that there were "no records (e.g. invoices, vouchers, checks) (provided) to support (payments made to staff relating to reimbursement) for expenses incurred for insurance and out-of-pocket payments..." Point of fact, ERCDC provided countless invoices, cancelled checks and vouchers to members of the audit team during the field work process which it appears the auditors have disregarded or failed to review. Our records indicate the documentation was provided. It is less clear that the documentation was given due consideration as required by the audit protocol.

* Comment 3

We renew our challenge to the auditors' suggestion that the reimbursements are suspect or inherently flawed because "such reimbursements are not addressed by ERCDC policy (handbook)." As shared with the auditors, the employment agreements of both the Executive Director and the Controller clearly provide that "(the) Employer agrees to pay one hundred percent (100%) of family health, catastrophic coverage, dental and prescription coverage (including related copayments and deductibles), long term care, life and disability insurance". (See: Attachment D) Note that the contract provision does not require that the employees participate in a ERCDC offered health care plan.

These employment agreements were duly approved by the governing Board (See: Attachment E). Clearly, the Board approved employment agreements both "support" <u>and</u> "provide for" this specific benefit. That the benefit is not referenced in the employee handbook does not compromise in any way the integrity of the "reimbursement mechanism" (or more appropriately characterized "fringe benefit") as the auditors would suggest. The particulars of management fringe benefits are generally reserved to the employment agreement and often the subject of confidential negotiation, as auditors might presume.

We must also challenge the auditors' assertion that the arrangement was not otherwise available to other employees. Point in fact, employer reimbursement for participation in a previous employer or "outside" health insurance plan was also made available to a special education classroom teacher

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(7/25/2014, FY 2015) who required "high risk pregnancy" coverage which was not offered under the ERCDC plan.

We take particular exception to the auditors' allegation that the Controller had asserted that certain "accommodations were made" for two employees "because they were part of ERCDC's management." The auditors have distorted and mischaracterized the substance of that conversation in which the Controller sought to explain that the terms of certain individuals' employment arrangements provided for such contribution modifications.

While we note the auditors' acknowledgement that ERCDC clearly provided substantial documentation in support of these challenges (employment contracts; Board of Directors meeting minutes), we must challenge the auditors apparent dismissal of the value of these documents and clarify that the employment contracts did, in fact, apply to the audited period by extension since the Board minutes clearly reference approval of the audit period contracts.

Lastly, we challenge the auditors' claim that "the benefits in question were not afforded to all employees" and suggest that the auditors' have based their disallowance upon a notion of "being afforded", when the Reimbursable Cost Manual clearly requires application of the principle of proportionate similarity. As previously shared with the auditors, outside accountants had attested to the legitimacy of the "100% health care cost payment" arrangement (See: Attachment F) as standard practice in soliciting and retaining high management staff. Such arrangements – or fringe benefits – are reimbursable within the parameters of the RCM, ERCDC would agree. Accordingly, any disallowance associated with this benefit arrangement should be limited to the purported "excess" above other employee benefit levels or percentages and not, as proposed here, subject to wholesale disallowance in the entirety. Such an approach inappropriately and disproportionately disadvantages those individual benefit recipients. Consistent with NYSED's own policies governing treatment of "excesses" as related to executive compensation, for example, only that portion of compensation in excess of the median compensation is disallowed during the rate setting process, and not, as proposed here, the totality of the expense.

Time and Attendance

We challenge many of the mischaracterizations presented in the Draft Report relating to staff time and attendance.

*
Comment
4

30 Minute Departures

More specifically, as relates to the auditors' finding that staff "left 30 minutes early", we again assert that while the standard work day is 7 hours, many staff reserve their "lunch period" until the end of the work day. It is not uncommon in the educational field to reserve the allowable lunch period until the end of the standard work day especially when the class schedule of a morning 2 ½ hour program ends immediately before the commencement of the afternoon 2 1/2 hour program effectively eliminating the potential for a noon-hour lunch period or where the class schedule is a full 5 hours.

We reassert our belief that the auditors have misperceived these appropriately "clocked out" lunch break periods at the end of the work day as "early departures". Each of the identified employees worked a standard work day less the appropriate 30-minute lunch break period.

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We invite the auditors to confer with representatives of the NYSED rate setting unit to confirm that only recently did NYSED clarify through revisions to the RCM the expectation that staff's lunch periods are not reimbursable blocks of time. Knowing that this "clarification" was contrary to field practice, NYSED confirmed that current practice could continue (more specifically, including the "lunch period" within the calculation of the work day) without sanction or a forced reduction in the calculation of an individual staff person's FTE. Accordingly, any finding which alleges a "reduced" work day is baseless and contrary to NYSED policy.

Personal Sick Leave

We do not challenge the auditors' finding that a number of employees were granted leave beyond the standard allotment for personal reasons or illness. While ERCDC's policies do establish certain limits to employee paid leave, ERCDC has refined its protocols to assurance leave in excess of the allowable limit will be appropriately treated as unpaid leave.

"Mis-days"

ERCDC reasserts its initial challenge to the auditors' conclusion that time associated with an employee's failure to "swipe out" should be disallowed especially where, as here, independent verification of continued attendance during the balance of the work day has been provided. Time stamped logs and supervisors' review of time records substantiate the continued attendance of these individuals, as also the case of the employees similarly identified in the initial preliminary audit report. ERCDC has provided the auditors Easy Trac entries, session notes and supervisor initialed time records in support of the entirety of the work day, notwithstanding the employees omitted "swipe out", sufficient to challenge the finding.

* Comment 5

"Blue Days"

Here too, for all of the reasons provided in our August 19th and September 27th responses, ERCDC reasserts its challenge of disallowances associated with omitted "swipe out" records resulting from the preparation of payroll. As supported by substantiating records including Easy Trac entries, session notes and supervisors' attestation and visual confirmations, each of the identified employees' time extended through the standard work day and should be properly remunerated.

Controller's Title and Responsibilities

ERCDC takes particular exception to the auditors' assessment of the duties and responsibilities of the Controller. ERCDC challenges the auditors' characterization of the tasks performed by the Controller as insufficient to warrant the title or compensation associated with the position code 603 – Controller, Director of Finance or such other individual responsible for overall fiscal management of ERCDC. We believe that the mischaracterization is the result of a misunderstanding of the level of the Executive Director's involvement in the fiscal management of the agency. More specifically, we believe that the Executive Director's review and monitoring of the agency's fiscal matters has been misconstrued as assuming primary responsibility for such matters. Point in fact, ERCDC's own internal controls, policies and procedures emphasize the agency's commitment to segregated responsibilities to assure operational integrity.

* Comment 6

GREENBERG TRAURIG, LLP ▪ ATTORNEYS AT LAW ▪ WWW.GTLAW.COM

We are disappointed that after several lengthy interviews, detailed review of substantial work product and agency policies and procedures, the auditors challenge the comprehensiveness of the Controller's duties and responsibilities. As the attached internal control statement reflects (See: Attachment #G) the Controller's responsibilities include, but are not limited to:

- ✓ preparation of budget reports and internal financial statement and schedules including the balance sheet and profit & loss statement;
- ✓ review and validation of invoices;
- ✓ bank reconciliations;
- ✓ posting to the general ledger as summarized in the trial balance;
- ✓ monitoring of cash flow; and
- ✓ processing of payroll, accounts receivable and accounts payable.

Moreover, many of the auditor's assertions are simply inaccurate. The Executive Director does not "handle the trial balance". It is the Controller who posts all entries to the general ledger that is summarized in the trial balance.

The Controller does in fact prepare the P&L statements based upon Controller entries into the system.

The Executive Director does not "handle" financial positions and functional expenses, but rather these statements are generated by Controller entries into the accounting record system.

The Controller does manage payroll, as well as revenue and the entry of service data into the NYC "certified monthly roster" (CMR) which tracks services provided and enrollment – key fiscal management responsibilities.

It appears that the auditors have attributed a significant portion of the Controller's tasks performed to the Executive Director based, apparently, on his oversight role and responsibilities. All statements, fiscal entries, accounting determinations and related fiscal duties are performed in the first instance by the Controller. Any involvement in these day to day fiscal management duties by the Executive Director is limited to furtherance of his general management oversight responsibilities.

ERCDC welcomed the opportunity to crosswalk the duties and responsibilities of the Controller as outlined in the Internal Control Statement with actual tasks performed beyond the sampled 24 days, as it appeared that either the documents provided did not adequately capture the depth of the Controller's tasks performed, or the auditors did not adequately value the information provided. The attached document (See: Attachment #H) provides a detailed description of the daily activities in which the Controller engaged on the specific 24 days sampled by the auditors. ERCDC provided nearly 350 pages of documentation, including a detail of the duties performed within that 24-day period and beyond, reflecting activities as a finance director, payroll director, accounts receivable director and accounts payable director, among other conjoined positions. We believe the auditors' may have focused on a single task performed on those days and ignored the substantial tasks performed in addition to the "one specific" task for which the auditors' requested supporting documentation.

Simply stated, we believe the Controller's responsibilities are wholly consistent with those of a Controller, as substantiated by records and work product. We further believe that the auditors have misunderstood the role of the Executive Director in the day to day management of the agency's fiscal operations and misperceived his comprehensive understanding of these matters and painstaking oversight as direct involvement to the degradation of the Controller's performed duties.

Allocation of Staff's Time Between Programs

Allocation of 1:1 Employees

We do not challenge the auditors' restatement of the principles of the Reimbursable Cost Manual which directs that all costs and expenses associated with 1:1 aide personnel must be reported to the 1:1 aide cost center regardless of whether those individuals are redeployed to other programs when the 1:1 aide's assigned student is absent.

We do challenge, however, the auditors' calculation of disallowance based solely on the number of school session days. ERCDC's employment policies reflect an appropriately standard annual employment period. Direct care staff provide services over a 46-week school year, as contemplated by the RCM. ERCDC compensates its direct care staff over a 52-week period, however, as also contemplated by the RCM. The intervals of payment (52) are <u>not</u> expressly aligned with the number of weeks for which such payment is made. We do not believe this distinction was recognized in the auditors' calculations. * Comment 7

Housekeeping and Maintenance Costs

As a point of clarification, we believe the auditors may have misunderstood the Executive Director's explanation of a prior SED accountant's technical assistance regarding how to allocate certain costs. Requests made to SED RSU representatives by ERCDC for technical assistance did not include allocation of housekeeping and maintenance costs.

We do not challenge the auditors' assertion that, with one exception, ERCDC did not properly allocate the salary costs of certain housekeeping and maintenance personnel consistent with such individuals' defined responsibilities. Of the five personnel identified, S.B. was responsible for cleaning classroom space with associated student bathrooms, and designated therapy rooms. (See: Attachment I – Cleaning and Maintenance, Duties and Responsibilities)

The attached duty descriptions clearly identify that portion of the premises S.B. was responsible to clean, exclusively. Accordingly, the salary costs of S.B. are appropriately allocated primarily to the classroom cost center (9100 Pre-K). We respectfully request reconsideration of the proposed reallocation consistent with the actual services provided as supported by the provided job descriptions and confirmed upon interview of the individual whose task performance has been challenged by the auditors.

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Allocation of SEIT Personal Services Costs

ERCDC does not challenge the auditors' finding that through a clerical error, a portion of a singular SEIT employee's salary was inadvertently allocating to the 9100 cost center. ERCDC has strengthened its internal protocols to avoid such errors in the future.

Other than Personal Service Costs

Consultants

We challenge the auditors' valuation of indirect/non-direct care activities engaged in by certain therapy independent contractors upon which the consultant service disallowance is based, in large part. As discussed in great detail in our preliminary report responses, was well as during the exit conference, and thereafter, clinical practitioners provide both direct and indirect services.

* Comment 8

ERCDC also believes that a fuller explanation of the clinical service providers' agreement may be warranted. It is a mischaracterization to describe the service fee as reimbursement of direct services only. As the attached agreement reflects, provision of both direct and non-direct or related activities is clearly contemplated (See Attachment J), with reference to both the provision of the clerical service, as well as the non-direct activities of maintaining progress notes and reports and data collection through Easy Trac, the City's computerized data input system. We believe the auditors may have significantly underestimated time spent on these tasks by only acknowledging the Easy Trac data input time and none other.

ERCDC consultants provide 5 full hours of direct service within the standard 7 hour work day, allowing 2 full hours of non-direct/related activities. This proportion of direct/non-direct is reflected throughout NYSED cost reporting devices which anticipate a 35 hour work week (7x5), in full acknowledgement that students are only present for 5 of those 7 hours whether through a full day classroom model (5 hours) or 2 back-to-back ½ day session classes (2 ½ x 2). Thus, the program models contemplate that both pedagogical and clinical staff will be engaged in activities to the benefit of the student which are both direct and non-direct in the course of a standard 35 hour work week, and, importantly, will be compensated accordingly.

We believe the method by which the clinical staff reflected their time in submitted invoices may have unnecessarily complicated the auditors' assessment of time spent on task. Clearly, clinical staff attendance records, progress notes and entries into the Easy Trac system attest to the fullness of the work day. By ERCDC's calculations, a caseload of 10 students per day (10 sessions) requiring 9 minutes of non-direct/related activity per student per day would approximate 90 minutes per day of time on task beyond the 5 hours of direct service. When then allowing for a ½ hour lunch break, the full 7 hour day has been accounted for.

We believe that a re-examination of the consultant services documentation against the framework presented above will compel the elimination of the proposed disallowances.

Further, as related to the number of sessions per week, we believe the auditors may have misread the attendance sheet entries which led to an exaggerated number of "sessions provided" per school day and per week (per a child's IEP). The form provides 4 designations: X, A, P and H. Only data provided under the "X" designation on the form should be considered when calculating "Number of Sessions".

Carmen Maldonado
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"X" denotes "session provided"; "A" denotes "student absence"; "P" denotes "provider absence" and "H" denotes holiday/school closure. By way of illustration, data entered for 1/9 and 1/22/2014 if properly assessed by disregarding "A" or "P" or "H" entries, would reflect the appropriate number of services per week in full compliance with the students IEP. We made special note as well of O.C. who was added to K.D.'s caseload in January 2014. K.D. erred in identifying the required services as 2 x 30 when, in fact, the IEP mandated 3 x 30 which is the number of services duly provided.

A similar analysis would eliminate the proposed disallowances associated with "18 instances of days where the OT provided more than 10 sessions per day" since only data provided under the "X" designation should be counted and not the "A" / "P" / "H" entries. By way of illustration, S.M. did not provide 12 sessions on July 5th and 12th in excess of the anticipated 10 sessions. In fact, 5 sessions were provided, and 7 entries were made to reflect the student's absence. (See: Attachment K)

We believe a re-examination of the form will support our challenge.

Other OTPS Items

ERCDC must challenge a number of the assertions contained in the Draft Report relating to the adequacy of certain supporting documentation provided to the auditors; more specifically:

- ERCDC did, in fact, provide the auditors with an invoice for certain legal services, the detail of which appropriately identified the actual work performed (the audit confirmation letter);

- ERCDC did, in fact, provide supporting documentation for nutritional snacks which were for instructional purposes;

- ERCDC did, in fact, provide the auditors with ample indicia of staff attendance at an IAC conference, including ID badge, literature and notes from the presentations, together with an attestation by the conference host that "no certificates of completion" were provided at the event; and

- ERCDC did, in fact, provide the auditors with a full explanation of the "bar and grill" invoice; specifically, the purchase of "bite-size sandwiches" for 96 students for a holiday celebration.

* Comment 9

Other Matters

We take final exception to the auditors' assertion that ERCDC failed to demonstrate its purchase of clinical services was "most economical and/or appropriate". We believe the auditors may have misunderstood a point made by the Executive Director in his explanation of the vendor selection process in which ERCDC engaged. In the interest of full disclosure, the Executive Director shared with the auditors the fact that a previous ERCDC employee was now a principal owner of the vendor corporation. The auditors appear to have misinterpreted this situation as warranting concern, perhaps conjecturing that the prior employment relationship was the primary consideration in the vendor selection process.

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To the contrary, ERCDC provided ample materials to the auditors attesting to the appropriateness of the vendor's selection, including documentation of ongoing communications regarding pricing surveys, together with a compelling comparable of nearly double for price paid by ERCDC.

ERCDC believes the totality of these materials provides ample assurance that the clinical services were obtained at the best price, to the benefit of both the agency – which derives no benefit from excessive payments to vendors – and to the State.

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We appreciate the opportunity to reaffirm our challenges to certain findings contained within the Draft Report and to provide the appropriate context within which we believe those proposed findings should be correctly viewed.

Very truly yours,

GREENBERG TRAURIG, LLP

Pamela A. Madeiros

PAM/hae
Attachments
ALB 2005554v1

CC: Commissioner Elia, NYSED
Thalia Melendez, NYSED
Suzanne Bolling, NYSED
James Kampf, NYSED
Joseph Smith, OSC
Brian Zimmerman, ERCDC

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State Comptroller's Comments

1. The Manual states, "Costs will not be reimbursable on field audit without appropriate written documentation of costs." ERCDC did not provide supporting documentation that several of the expenditures examined were reasonable, necessary, directly related to the special education program, and sufficiently documented. As a result, we recommended disallowances for personal service costs where ERCDC did not maintain required supporting documentation.
2. ERCDC did not comply with the Manual's requirements for reimbursement of pension expenses. The Manual requires that such benefits be proportionally similar to those received by other classes or groups of employees. The documents submitted as part of the 30-day response to our draft report did not provide any additional information relevant to the basis of the disallowance.
3. ERCDC did not directly pay for the health insurance premiums or the out-of-pocket expenses claimed by the ED and Comptroller. Instead, these costs were paid directly by the ED, who was reimbursed through the payroll. Further, the "countless invoices, cancelled checks and vouchers" provided to members of the audit team supported the costs that ERCDC paid for other ERCDC employees, but not the ED and the Comptroller. Moreover, there was no support that this particular benefit was afforded to any other employees, and as such, it was not proportionately similar as required by the Manual for reimbursement.
4. The auditors requested documents to support the hours worked by staff. In the absence of time clock entries (which ERCDC management stated is their official timekeeping method) or alternative documentation, we concluded the expenditures in question were not supported.
5. ERCDC's reply that it provided alternative supporting documentation for dates when certain employees did not "swipe out" at the end of the day is incorrect. In fact, we were told that the employees in question could not clock out because the time clock was not working. However, this explanation is unsatisfactory, as during this same time period other ERCDC staff did manage to clock out. We brought this issue to the ED's attention, asked if alternative support for hours worked was available, and were advised that no provisions were made when the time clock was not working.
6. As detailed on page 8 of this report, we based our finding on the requirements of the Manual, which states, in part, "Compensation to all individuals who have a financial interest in the program including … family members or others who are also program employees must be commensurate to actual services provided as appropriately qualified employees or consultants." Based on the available evidence, this requirement was not met. Moreover, the 350 pages of additional documents provided to support the Comptroller's duties consisted primarily of copies of payroll registers and bills paid, along with several copies of "certified monthly rosters." However, no information is included that would support a change in the disallowance.
7. Our recommended disallowance is based on ERCDC non-compliance with the applicable provisions of the Manual. In addition, as shown on page 12 of this report, the impact of the revised allocation is minimal because $9,221.50 of the $13,203.51 in costs were moved from the SC to SEIT. The disallowance of $2,008 is for Evaluations and agency

administration costs.

8. ERCDC's ED paid a consultant, SPOTS, $57,235 for occupational therapy sessions in 2013-14. The ED stated that the benefit of obtaining services from a vendor that was owned by an occupational therapist who, at that time, was employed by ERCDC, was that ERCDC paid only for direct services. This was also ERCDC's justification for not obtaining bids for the services as required by the Manual. We met with the ED to advise him that, based on his prior explanation, only direct time (i.e., sessions) would be allowed. At that time, he indicated that time should also be allowed for entering notes into EasyTrac after the sessions. The auditors reviewed the comments in EasyTrac and made the appropriate adjustments.
9. We reduced the amounts of the recommended disallowance for OTPS costs in our report based on the additional documentation provided.
10. The Manual states that: "When applicable, competitive bidding practices should be used in conformance with the Purchasing Handbook." According to the Purchasing Handbook, bids are required for contracts of $35,000 (effective November 12, 2009). The payments to the vendor totaled $57,235 during the 2013-14 fiscal year. Moreover, ERCDC did not have documents to support the selection process. In regards to the "former employee," auditors did not misinterpret this situation, as during the 2013-14 year (when the services were purchased from the vendor), the "now principal owner of the vendor corporation" was an employee of ERCDC.