New York State Comptroller
THOMAS P. DiNAPOLI

# Abilities First, Inc.: Compliance With the Reimbursable Cost Manual

## State Education Department

Report 2022-S-23 | **February 2023**

Spotlight on Education

# Audit Highlights

## Objective

To determine whether the costs reported by Abilities First, Inc. (AFI) on its Consolidated Fiscal Report (CFR) were properly calculated, adequately documented, and allowable under the State Education Department's (SED) guidelines, including the Reimbursable Cost Manual (RCM) and the Consolidated Fiscal Reporting and Claiming Manual (CFR Manual). The audit covered expenses reported on AFI's 2018 and 2019 CFRs for the fiscal year ended June 30, 2019.

## About the Program

AFI is a not-for-profit special education provider located in Wappingers Falls, serving students from three counties in the Mid-Hudson region. Among other programs, AFI is authorized by SED to provide preschool special education services to children with disabilities who are between the ages of 3 and 5 years at four different locations. AFI is reimbursed for these services through rates set by SED. The reimbursement rates are based on financial information, including costs, that AFI reports to SED on its annual CFR. To be eligible for reimbursement, reported costs must comply with RCM requirements. For the fiscal year ended June 30, 2019, AFI reported more than $4.41 million in reimbursable costs for its Preschool Special Class – over 2.5 hours per day, Preschool Integrated Special Class – over 2.5 hours per day, and Preschool Integrated Special Class – 2.5 hours per day (collectively referred to as the Programs).

## Key Findings

For the fiscal year ended June 30, 2019, we identified $236,209 in ineligible costs reported by AFI on its CFRs for the Programs. The ineligible costs included:

- $164,406 in personal service costs consisting of $157,881 in costs that were not appropriately allocated to the Programs and $6,525 in other ineligible costs.
- $71,803 in other than personal service costs consisting of $49,025 in ineligible costs, $22,544 in unsupported costs, and $234 for SED rate adjustments.

## Key Recommendations

**To SED:**

- Review the recommended disallowances identified by our audit and, if warranted, make the necessary adjustments to the costs reported on AFI's CFRs and to AFI's tuition reimbursement rates.
- Remind AFI officials of the pertinent SED requirements that relate to the deficiencies we identified.

**To AFI:**

- Ensure that costs reported on annual CFRs fully comply with SED's requirements and communicate with SED to obtain clarification as needed.

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

February 13, 2023

Betty A. Rosa, Ed.D.
Commissioner
State Education Department
State Education Building
89 Washington Avenue
Albany, NY 12234

Jeffrey Fox, Ph.D.
President/Chief Executive Officer
Abilities First, Inc.
167 Myers Corners Road, Suite 202
Wappingers Falls, NY 12590

Dear Dr. Rosa and Dr. Fox:

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 the 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 costs submitted by Abilities First, Inc. to the State Education Department for the purpose of establishing the preschool special education tuition reimbursement rates used to bill public funding sources that are supported by State aid payments. 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.

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 report, please feel free to contact us.

Respectfully submitted,

*Division of State Government Accountability*

# Contents

# Glossary of Terms

| Term | Description | Identifier |
|---|---|---|
| SED | State Education Department | *Auditee* |
| | | |
| AFI | Abilities First, Inc. | *Service Provider* |
| CFR | Consolidated Fiscal Report | *Key Term* |
| CFR Manual | Consolidated Fiscal Reporting and Claiming Manual | *Policy* |
| GSA | U.S. General Services Administration | *Federal Agency* |
| OTPS | Other than personal service | *Key Term* |
| Programs | Preschool Special Education Classes and Preschool Integrated Special Classes | *Key Term* |
| RCM | Reimbursable Cost Manual | *Policy* |

# Background

Abilities First, Inc. (AFI) is a not-for-profit special education provider located in Wappingers Falls, serving students from three counties in the Mid-Hudson region. AFI is authorized by the State Education Department (SED) to provide preschool special education services to children with disabilities who are between the ages of 3 and 5 years at four different locations. During our audit period, AFI operated three rate-based preschool education programs for 118 children: Preschool Special Class – over 2.5 hours per day, Preschool Integrated Special Class – over 2.5 hours per day, and Preschool Integrated Special Class – 2.5 hours per day (collectively referred to as the Programs).

The counties that use AFI preschool special education services pay tuition to AFI using reimbursement rates set by SED. The State, in turn, reimburses the counties for a portion of the tuition paid. SED sets the special education rates based on financial information, including costs, that AFI reports to SED on its annual Consolidated Fiscal Report (CFR). Costs reported on the CFR must comply fully with the guidelines in SED's Reimbursable Cost Manual (RCM) regarding eligibility and documentation requirements and must meet the reporting requirements prescribed in the Consolidated Fiscal Reporting and Claiming Manual (CFR Manual). For the fiscal year ended June 30, 2019, AFI reported more than $4.41 million in reimbursable costs for the Programs.

# Audit Findings and Recommendations

According to the RCM, costs reported on the CFR are considered for reimbursement if they are reasonable, necessary, directly related to the special education program, and sufficiently documented. For the fiscal year ended June 30, 2019, among other issues, we identified $236,209 in costs that AFI reported on its CFR that did not comply with SED's requirements for reimbursement. The ineligible costs include $164,406 in personal service costs and $71,803 in other than personal service (OTPS) costs. A summary of ineligible costs is presented in the Exhibit at the end of this report.

## Personal Service Costs

Personal service costs, which include all salaries and fringe benefits paid or accrued to employees on the provider'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). For the school year ended June 30, 2019, AFI reported $3.69 million in personal service costs charged to the Programs. We selected a judgmental sample of various personal service categories totaling $2.35 million and identified $164,406 in expenses that were not allowable under SED's requirements.

### Program Salary Allocations

According to the RCM, 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, such as payroll records or time studies, that reflect the hours used in the allocation. AFI incorrectly allocated $157,881 ($125,911 in salaries and $31,970 in fringe benefits) to the Programs for administrative, non-program, program, and maintenance staff as follows:

- AFI directly charged administrative staff salaries to the Programs using an allocation method based on department salary totals, which is inconsistent with CFR Manual requirements. This resulted in $77,606 ($62,182 in salary and $15,424 in fringe benefits) of additional expenses allocated to the Programs than if they had been properly reported on the CFR as administrative expenses.
- The salaries and associated fringe benefits for three employees were partially allocated to the Programs, despite time sheets indicating they were working in AFI's day treatment and school-age programs, resulting in reimbursable expenses being overstated by $50,763 ($40,826 in salaries and $9,937 in fringe benefits). AFI officials stated that the allocation of salaries for these individuals to the Programs was based on services provided to the Programs; however, they did not provide documentation, as required by the RCM, to support this.
- AFI did not provide documentation to support $21,370 in personal service expenses ($15,336 in salaries and $6,034 in fringe benefits) for its maintenance department that was allocated to the Programs. AFI uses the actual maintenance department hours spent working on various programs to

allocate the maintenance department's personal service expenses; however, according to AFI, limitations of the time reporting system used during our scope period did not allow for the accounting of hours worked by the maintenance staff for part of the scope period. AFI officials stated they have since switched to a new time reporting system for maintenance hours.

- AFI officials acknowledged they erroneously reported $6,314 in expenses ($5,167 in salary and $1,147 in fringe benefits) during the cost reporting period for one employee. This was a result of using a non-compliant time study to allocate the employee's salary to various programs.
- The CFR charges to the Programs for certain employees who worked in multiple departments were not always supported by the employee's time cards and, in some cases, AFI's allocation percentages for the department's salary expenses. This resulted in the Programs' costs being overreported by $1,718 (overreported by $2,312 in salaries and underreported by $594 in fringe benefits).
- AFI officials acknowledged $110 in payroll expenses ($88 in salary and $22 in fringe benefits) were erroneously charged to the Programs because of a mathematical error related to accruals.

## Ineligible Expenses

AFI submitted $6,525 in costs ($4,735 in salaries and $1,790 in fringe benefits) that were ineligible for reimbursement because they were not in compliance with RCM requirements.

### Bonuses

According to the RCM, performance bonuses are reimbursable only for direct care titles. Of the $69,941 in bonus payments reviewed, $6,032 ($4,377 in salary and $1,655 in fringe benefits) was allocated to the Programs. We found $6,006 in bonuses paid to AFI executives not in direct care titles. Additionally, AFI administrative staff were paid $300 in referral bonuses in 2019, of which $26 was allocated to the Programs. AFI officials acknowledged that these amounts were misreported as allowable expenses.

### Automobile Allowance

AFI inappropriately reported an automobile allowance paid to its Chief Executive Officer as an allowable cost on its CFR. According to the RCM, costs of a personal nature, such as the personal use of a car – known as perks – are not reimbursable. Additionally, auto repair, depreciation, insurance, rental, and maintenance costs incurred by employees for privately owned vehicles are not reimbursable. Of the $4,560 in reported automobile salary costs AFI reported on its CFR, $373 ($271 in salary and $102 in fringe benefits) was allocated to the Programs. AFI officials disagreed and stated that automobile allowance costs were reported on the CFR as salary and compensation, which is reimbursable. However, while the expense was paid as salary and compensation, the Chief Executive Officer's employment agreement explicitly notes the amount is for a vehicle allowance.

### Excess Payments

The RCM limits which position titles can receive reimbursable compensation in excess of one full-time equivalent unit. AFI paid one non-direct care employee, with a non-excluded position title, in excess of this limit by $1,383, of which $120 ($87 in salary and $33 in fringe benefits) was allocated to the Programs.

# Other Than Personal Service Costs

For the fiscal year ended June 30, 2019, AFI reported $727,532 in OTPS costs charged to the Programs. We selected a judgmental sample of various categories totaling $682,812 and identified $71,803 in OTPS expenses that were not allowable under SED's requirements.

## Ineligible Costs

According to the RCM, costs must be necessary and directly related to the special education programs. The RCM states property rental costs must be based on actual documented rental charges, and interest expenses are reimbursable only when there are corresponding payments of principal and no less-than-arm's-length loans during the loan repayment period. According to the RCM, the following expenses are not reimbursable: fundraising costs, costs incurred for food provided to staff, and gifts. Travel expenses of non-employees are not reimbursable, and logs must be kept by each employee with supervisory approval for the associated travel expense to be reimbursable. Costs incurred for the entertainment of employees, activities not related to the Programs, or any related items such as meals, lodging rentals, and transportation are not reimbursable. Lastly, reimbursement for in-state and out-of-state meals and lodging are limited to the U.S. General Services Administration (GSA) allowance rates. For the fiscal year ended June 30, 2019, we found that AFI charged $49,025 in ineligible costs to the Programs on its CFRs. These costs included:

- $40,777 in costs associated with future lease expenses for two building leases.
- $5,108 in payments made on an interest-only capital line-of-credit loan while also having an outstanding less-than-arm's-length loan.
- $1,259 in travel-related costs that were inappropriately allocated or inadequately documented for consultants, unrelated programs, or fundraising or that exceeded federal reimbursement limits.
- $846 in costs unrelated to the Programs, including costs for other programs, such as AFI's Foundation, and for programs related to the Office for People With Developmental Disabilities.
- $504 for two expenses charged to the incorrect CFR reporting period.
- $166 in late fees not directly related to the Programs.

- $136 in fundraising costs.
- $131 for food provided to staff and gifts.
- $73 for medical expenses not necessary for the operation of the Programs.
- $25 for fraudulent credit card expenses unrelated to the Programs.

AFI did not challenge the audit team's determination that these costs were not in compliance with RCM guidelines, with the exception of the future lease obligation costs. While AFI officials acknowledged the RCM does not allow for the reimbursement of future lease obligations, they contended that these costs adhere to generally accepted accounting principles, as required by both the RCM and the CFR Manual, and that it isn't clear which directive should take precedence.

## Unsupported Costs

According to the RCM, costs will be considered for reimbursement provided they are reasonable and sufficiently documented. Entities operating approved programs are required to retain all documentation supporting reported data for 7 years, or in some cases longer, such as with information relating to the acquisition of fixed assets used by education programs. Additionally, entities must use allocation methods that are fair, reasonable, and documented. Furthermore, the RCM states that all less-than-arm's-length transactions are to be reimbursed using actual documented costs of the connected party, and that it is expected that such documentation showing the actual costs to the connected party will be made available upon audit or review.

For the fiscal year ended June 30, 2019, we found that AFI charged $22,544 in unsupported OTPS costs to the Programs on its CFR for depreciation, maintenance allocation, and other undocumented costs. These include:

- $9,871 in depreciation costs of several fixed assets that did not have the required supporting documentation.
- $7,081 for related-party, property damage, legal, and staff reimbursement costs with inadequate or no supporting documentation.
- $5,592 in maintenance department OTPS cost allocations for which AFI was unable to provide support due to limitations of the time reporting system it used.

AFI officials disagreed with the related-party findings, stating they were based on "inartful" general ledger expense descriptions. While the general ledger descriptions of these expenses appear ineligible, AFI also did not provide adequate supporting documentation as required by the RCM. Additionally, AFI disagreed with the finding for repair costs associated with property damage. Officials stated that the repair costs were more reasonable and cost effective than submitting an insurance claim, which would be below the deductible threshold; however, they did not provide documentation to support this statement.

## SED Rate Adjustments

In order to calculate a provider's rate, SED must manually adjust expenses marked by providers as non-allowable on their CFRs. SED did not use the correct 2018 CFR to calculate the administrative expense rate adjustment for amounts identified by AFI as non-allowable, resulting in $3,737 being incorrectly included in administrative costs, of which $234 was included in the Programs.

# Other Matters

## Collaborative Agreement

According to the RCM, costs are considered for reimbursement provided such costs are reasonable, necessary, and directly related to the special education program. Additionally, the RCM states that expenses are not reimbursable if they are for services already funded, wholly or in part, by taxpayer funds. For the fiscal year ended June 30, 2019, AFI had a collaboration agreement for $20,683 with another provider for the required complement of general education students needed for an integrated setting required by one of the Programs. The agreement outlines the provision of certain services by each provider and includes services applicable to general education students that are not reimbursable costs for the Programs. However, costs were not itemized on the agreement; therefore, we could not determine if any costs AFI claimed on its CFR were for non-reimbursable services, and AFI did not provide documentation that would support itemization. Further, the other provider was also an SED-approved preschool special education provider, and without proper documentation, we were unable to determine if any of the expenses submitted by AFI were already reimbursed by SED through the other provider's integrated preschool special education program.

## Competitive Bidding

According to the RCM, competitive bidding practices should be used by all providers when applicable, and the selection of professional services must be done at a minimum of every 5 years through solicitation of competitive bids. The RCM specifies that bidding documentation must be kept on file by the entities operating the program, and that the entities will need to justify that the consultant hired was the most economical and/or appropriate choice available for a particular service. In response to our request for vendor selection, prevailing rate, and equipment rental cost analysis documentation for certain transactions in our sample, AFI did not provide sufficient documentation. AFI officials should make use of competitive bidding to ensure that the prices paid for select services and products are the most cost efficient and appropriate for their business, as required by the RCM.

# Recommendations

**To SED:**

1. Review the disallowances identified by our audit and, if warranted, make the necessary adjustments to the costs reported on AFI's CFR and to AFI's tuition reimbursement rates
2. Remind AFI officials of the pertinent SED guidelines that relate to the deficiencies we identified.

**To AFI:**

3. Ensure that costs reported on annual CFRs fully comply with SED's requirements and communicate with SED to obtain clarification as needed.

# Audit Scope, Objective, and Methodology

The objective of our audit was to determine whether the costs reported by AFI on its CFR were properly calculated, adequately documented, and allowable under SED guidelines, including the RCM and the CFR Manual. The audit covered expenses reported on AFI's 2018 and 2019 CFRs for the fiscal year ended June 30, 2019.

To accomplish our objective, we reviewed the RCM, CFR Manual, and related appendices that applied to the years we examined. We also evaluated the internal controls over the costs claimed and the schedules prepared in support of the CFRs submitted to SED. We reviewed AFI's CFRs for the 2 calendar years ended December 31, 2019, with a focus on costs for the fiscal year ended June 30, 2019, as well as relevant financial records for the audit period. We determined the data was sufficiently reliable and appropriate for use in accomplishing our objective. We interviewed AFI personnel and reviewed AFI's policies to obtain an understanding of its financial practices for reporting costs on the CFR. For personal service costs, we reviewed time records and support for a judgmental sample of employees based on the number of position codes worked, which CFR schedule they were charged to, the number of Programs their salary was attributed to, and the employee pay rate. We selected transactions utilizing pay codes for which we knew there to be detailed RCM criteria (e.g., bonus payments and senior executive perks) and reviewed supporting documentation. For OTPS costs, we selected a judgmental sample of costs claimed by AFI for reimbursement based on high risk (e.g., higher dollar amounts, related-party transactions, and costs that appeared not to be relevant to the Programs) to determine whether they were properly calculated, adequately documented, and allowable. Based on our sample design, we cannot project our results to the population as a whole.

# Statutory Requirements

## 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.

We conducted our performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objective. We believe that the evidence obtained 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. These duties could be considered management functions for purposes of evaluating organizational independence under generally accepted government auditing standards. In our professional judgment, these duties do not affect our ability to conduct this independent performance audit of SED's oversight and administration of AFI's compliance with the RCM and CFR Manual.

## Reporting Requirements

We provided a draft copy of this report to SED and AFI officials for their review and formal comment. We considered their comments in preparing this report and have included them in their entirety at the end of the report. In SED's response, officials agreed with the recommendations and indicated the actions they will take to address them. However, in their response, AFI officials disagreed with many of the proposed disallowances. Our responses to certain AFI comments are included in the report's State Comptroller's Comments.

Within 180 days after 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 where recommendations were not implemented, the reasons why.

# Exhibit

**Abilities First, Inc.**
**Schedule of Submitted and Disallowed Program Costs**
**for the Fiscal Year Ended June 30, 2019**

| Program Costs | Amount Reported on CFR | Amount Disallowed | Amount Remaining | Notes to Exhibit |
|---|---|---|---|---|
| Personal Services | $3,685,186 | $164,406 | $3,520,780 | A, E-G, R |
| Other Than Personal Services | 727,532 | 71,803 | 655,729 | A-D, H-Q, S-V |
| **Total Program Costs** | **$4,412,718** | **$236,209** | **$4,176,509** | |

# Notes to Exhibit

The following Notes refer to specific sections of the RCM that we 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 AFI's officials during the course of our audit.

A. RCM Introduction, page 3 – Costs are reimbursable provided that they are "reasonable, necessary and directly related to the education program." Costs must also have "adequate substantiating documentation" – with final costs being determined upon field audit. When the RCM is silent on the treatment of a cost, it should not be assumed that such costs are reimbursable or that the method of allocation is deemed appropriate without written approval.

B. RCM Section I.4.F.(7) – All less-than-arm's-length transactions will be reimbursed using actual documented costs of the owner or vendor.

C. RCM Section I.10.A – In determining reasonableness of a given cost, consideration will be given to whether the cost is of a type generally recognized as ordinary and necessary for the operation of the approved special education program.

D. RCM Section II – Costs will be considered for reimbursement provided such costs are reasonable, necessary, directly related to the special education program, and sufficiently documented.

E. RCM Section II.13.A.(4)(d) – Compensation beyond 1.000 FTE for non-direct care staff (excluding 100 Position Title Code series and Position Title Codes 505 and 605) will not be considered reimbursable in the calculation of tuition rates.

F. RCM Section II.13.A.(6) – Expenses of a personal nature, such as a residence or personal use of a car, are not reimbursable.

G. RCM Section II.13.A.(10) – Merit awards (or bonus compensation) are restricted to direct care titles/employees and those in the 100 Position Title Code series and Position Title Codes 505 and 605.

H. RCM Section II.14.A.(1) – Consulting fees shall not exceed the prevailing rate for such services at the time such costs are incurred, the documentation for which shall be maintained by the school. Solicitation of competitive bids must be done every 5 years.

I. RCM Section II.20.A – Costs incurred for entertainment of officers or employees or for activities not related to the program, or any related items such as meals, lodging rentals, transportation, and gratuities, are not reimbursable.

J. RCM Section II.22.C – Costs of food provided to any staff are not reimbursable.

K. RCM Section II.23 – Costs of organized fundraising to raise capital or to obtain contributions are not reimbursable.

L. RCM Section II.24 – Gifts of any kind are non-reimbursable.

M. RCM Section II.28.C.(5) – Interest expenses are reimbursable only when there are corresponding amortization/payments of principal – and if there are no loans/notes receivable from related parties (LTAL) during the entity's loan repayment period. Payments that represent "interest only" are not reimbursable.

N. RCM Section II.41.B.(2) – Rental costs of buildings and facilities are reimbursable if such occupancy costs are based on actual documented rental charges.

O. RCM Section II.59.D.(3) – Use of privately owned vehicles for program business by employees is reimbursable provided such use is documented and necessary. Auto repair, depreciation, insurance, rental, garage, and maintenance costs incurred by employees for privately owned vehicles are not reimbursable.

P. RCM Section II.59.F – Travel expenses of spouses, family members, or any non-employee are not reimbursable.

Q. RCM Section III.1 – Entities operating approved programs are required to retain all documentation supporting reported data related to the establishment of tuition rates for 7 years following the end of each reporting year. Information relating to the acquisition of fixed assets and any related financing arrangements and grants must be retained as long as the facility is used by any education program the provider operates if this period exceeds 7 years. Costs will not be reimbursable on field audit without appropriate written documentation of costs.

R. RCM Section III.1.A-B – Compensation costs must be based on approved, documented payrolls. Payroll must be supported by employee time records. 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 pursuant to Appendix L of the CFR Manual.

S. RCM Section III.1.E – Logs must be kept by each employee indicating the dates of travel, destination, purpose, mileage, and related costs such as tolls, parking, and gasoline.

T. RCM Section III.1.M.(2) – Entities operating programs must use allocation methods that are fair and reasonable. 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 7 years.

U. RCM Section III.2.B – The accrual basis of accounting is required for all programs receiving Article 81 and/or Article 89 funds.

V. RCM Section VI, Appendix C – Reimbursement for in-state and out-of-state meals and lodging is limited to the GSA allowance rates.

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

EXECUTIVE DEPUTY COMMISSIONER
(518) 473-8381
E-mail: Sharon.Cates-Williams@nysed.gov

February 2, 2023

Ms. Theresa Podagrosi
Audit Manager
Office of the State Comptroller
Division of State Government Accountability
110 State St, 11th Floor
Albany, NY 12236

Dear Ms. Podagrosi:

The following is the New York State Education Department's (SED) response to the draft audit report, 2022-S-23, *Abilities First, Inc. (AFI) - Compliance With the Reimbursable Cost Manual*.

Recommendation 1:

**"Review the recommended disallowances identified by our audit and, if warranted, make the necessary adjustments to the costs reported on AFI's CFRs and to AFI's 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:

**"Remind AFI officials of the pertinent SED requirements that relate to the deficiencies we identified."**

We agree with this recommendation. SED will continue to provide technical assistance whenever requested and will strongly recommend AFI officials avail themselves of our assistance to help them better understand the rules for cost reporting and criteria for cost reimbursement as presented in the CFR, Regulations, and the Reimbursable Cost Manual (RCM).

Furthermore, SED will alert AFI of online CFR training that is available on SED's webpage. SED recommends that all individuals signing the CFR certification statements, namely the Executive Director and Certified Public Accountant, complete this training. This training is a requirement for preschool special education providers upon approval and reapproval.

If you have any questions regarding this response, please contact Nell Brady, Director of the Rate Setting Unit, at (518) 474-1298.

Sincerely,

Sharon Cates-Williams

Sharon Cates-Williams

cc: Phyllis Morris
Christopher Suriano
Suzanne Bolling
James Kampf
Jerry Nestleroad
Jeanne Day
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January 27, 2023

Theresa Podagrosi
Audit Manager
Division of State Government Accountability
Office of the State Comptroller
110 State Street, 11th Floor
Albany, NY 12236-001

Re: State Education Department
Compliance with the Reimbursable Cost Manual
Abilities First, Inc.
Audit Report 2022-S-023
Draft Report

Dear Ms. Podagrosi:

We have reviewed the above-referenced Draft report relative to compliance with the Reimbursable Cost Manual and to determining whether the costs and expenses reported by Abilities First, Inc. (AFI) on the Consolidated Fiscal Report (CFR) for the calendar years 2018 and 2019 that formed the basis for the 2018-19 school year (July 1, 2018 to June 30, 2019) for preschool special education programs 9100, 9160, and 9165 were properly calculated, adequately documented, and allowable under the State Education Departments guidelines, including the Reimbursable Cost Manual (RCM) and the Consolidated Fiscal Reporting and Claiming Manual (CFR Manual). We welcome the opportunity to correct any potential error of fact set out in the Report, and to provide additional information which should be considered in the formulation of audit conclusions, in furtherance of the stated goals of encouraging and maintaining transparency and an open dialog throughout the audit process.

**Personal Service Costs**

**Program Salary Allocations**

- AFI respectfully challenges the auditors' finding as relates to certain specific employees in select job titles; specifically, as relates to $37,630, the title position of Quality Assurance staff is clearly a position with responsibilities that extend over several cost centers, including the education programming which derives a benefit from the duties performed. At a minimum, then, the salary should be allowable to the extent allocatable through application of ratio value.

Comment 1

- As relates to $40,826 in salary expenses incurred by the Training Coordinator, Nursing Coordinator, and Speech Coordinator, we acknowledge that the descriptor "home cost center" was set out on the employee timesheets, as required by the agency's payroll system, pending allocation of time based on FTE's, actual time spent, or ratio value as applicable.

  The salary of the Training Coordinator titled position was allocated by ratio value to each cost center which derived a benefit as each cost center required a measure of employee / staff / programs training.

Theresa Podagrosi
Office of the State Comptroller
Page 2

Accordingly, that portion attributable under ratio value to the educational program should be recognized as an allowable expense.

The salaries associated with the Nursing Coordinator and Speech Coordinator were reported based upon actual time spent in service to the educational cost centers, as these two titled positions performed duties for the exclusive benefit of the educational program.

Comment 2

- As shared with the audit team, certain administrative salary costs proposed to be disallowed, are, in fact, appropriately incurred salary costs exclusive to the preschool special education program. The subject individual performed duties of the Director of Preschool until April, 2019, then assumed responsibilities as Vice President of Education for the balance of the year. Accordingly, AFI reported the salary prior to the promotion to the preschool cost center, rather than allocate across all cost centers as befitting the subsequent promoted position.

Comment 3

- AFI does not challenge the auditors' finding that insufficient documentation was provided in support of $21,370 in personal service expenses ($15,336 in salaries and $6,034 in fringe benefits) for the agency's maintenance department as the maintained hour tracker used to calculate hours of work performed failed to provide disaggregated data per cost center as necessary to support reported allocations.

- AFI does not challenge that $5,167 in salary expenses and $1,147 in related fringe had been erroneously reported as within the cost reporting period.

- The agency does not challenge the auditors' findings that $88 in payroll related expenses and $22 in related fringe benefits were erroneously reported due to a mathematical error related to accruals.

- The agency does not challenge the auditors' findings that $483, $148, and $88 in payroll related expenses were erroneously reported.

- AFI does not challenge the auditors' findings that corrections were necessary to align employee time records with costs as reported to the extent of $2,312.

**Ineligible Expenses**

- **Bonuses**

AFI does not challenge the auditors' finding that certain bonus awards, while well deserved, were misreported as allowable expenses, to the extent of $6,032 ($4,317 in salary and $1,655 in fringe benefits). We note, however, that these bonuses were allowable expenses under reporting requirements for non-SED state agency funded programs. The disaggregation of the bonus amounts attributable exclusively to the SED programs was not possible, however, resulting in the reporting as a SED program expense. Any alternative reporting would have resulted in over-reporting of expenses in the affected non-SED cost centers.

- **Automobile Allowance**

AFI does challenge the auditors' finding that certain automobile allowances were ineligible for reimbursement. While we concede that expenses of a personal nature, such as the personal use of a car (known as perquisites / perks) are not reimbursable (RCM Section II (13)(A)(6)), the expense was reported as salary/compensation and therefore reimbursable, to the extent of $271.

Comment 4

Theresa Podagrosi
Office of the State Comptroller
Page 3

- **Excess Payments**

The agency does not challenge the auditors' finding that a specific non-direct care employee was paid in excess of a full-time equivalent to the extent of $87 in salary and $33 in fringe benefits.

**Other Than Personal Service Costs**

**Ineligible Costs**

- **Future Lease Value**

AFI challenges the proposed disallowance of $40,777 in future lease expenses as the reporting was consistent with both GAAP and the CFR Manual. AFI contends that their records followed GAAP Guidance prior to the adoption of ASU No 2016-02 which, as reflected in section 33.106, provided: A lessee should account for an operating lease by charging the lease payment to expense. Generally, rent expense under an operating lease should be recognized on a straight-line basis over the lease term however, even if payments are not made on a straight-line basis.

Section 7 of the 2018-19 CFR Manual states: Method of Accounting – CFR Core Cost Report Schedules The core cost reporting Schedules CFR-1 through DMH-1 of Full, Abbreviated and Article 28 Abbreviated Consolidated Fiscal Reports (CFRs) must be completed using accrual accounting in accordance with U.S. generally accepted accounting principles (U.S. GAAP).

AFI complied with the applicable provision of GAAP – the same provisions which are also referenced in the RCM. It would appear, then, that there are two distinct interpretations of which directive is controlling. AFI determined GAAP to be controlling, and reported the lease expenses through straight-line accounting.

Comment 5

Accordingly, AFI accurately reported the actual expense over the life of the lease. We respectfully request that the proposed disallowances be reconsidered.

- **Interest-Only Capital Line of Credit Loan**

AFI does not challenge the proposed disallowances of $5,108 related to payments for a working capital line-of-credit loan.

- **Travel**

AFI does not challenge the proposed disallowances of $1,259 in travel costs.

- **Unrelated to Program**

AFI likewise does not challenge the proposed disallowance of $846 related to certain costs.

- **Late Accruals**

AFI does not challenge the proposed disallowances of $504 in prior year accruals which had been inadvertently reported in the audit years.

- **Late Charges**

AFI likewise does not challenge the proposed disallowance of $166 related to late fees which were erroneously reported as a reimbursable expense.

- **Staff Food**

AFI does not challenge the proposed disallowance of $131 in staff associated meal costs which, while well deserved, are non-reimbursable.

- **Fundraising**

AFI does not challenge the proposed disallowance of $136 related to fund raising costs.

- **Medical Expenses**

AFI does not challenge the auditors' finding that $73 in medical expenses associated with a student's injury, while well-intended, represents a non-allowable cost.

- **Gifts, etc.**

AFI likewise recognizes that $49 in reported costs associated with staff gifts of appreciation and promotional items had been misreported as a reimbursable cost.

- **Fraud**

AFI does not challenge the auditors' finding that $25 in expenses associated with a fraudulent credit card charge was inappropriately reported as an allowable expense.

**Unsupported Costs**

- **Related party / Property damage / Other costs**

AFI must challenge the auditors' assertion that certain other "items" paid to a related party are ineligible for reimbursement based upon a perhaps inartful description on the general ledger.

AFI must also challenge the auditors' proposed disallowance of certain payments made related to incurred property damage which the auditors' assert may not have complied with applicable insurance claim protocols. Simply stated, the deductible threshold under the property insurance power is quite high such that payment of cost of repairs was deemed more cost effective than submission of a claim which would ultimately be deemed as below the deductible threshold. Therefore, adherence with the RCM deductible would prove unsuccessful and would, in fact, be less reasonable and less cost-effective than payment of the repair costs.

Comment 6

- **Amortization / Depreciation**

AFI does not challenge the auditors' proposed disallowance of $9,871 associated with amortized leasehold improvements, depreciated buildings, depreciated equipment, or depreciated.

Theresa Podagrosi
Office of the State Comptroller
Page 5

- **Maintenance Allocation**

AFI does not challenge the auditors' proposed finding that a modification to the maintenance hours tracking system failed to provide sufficient documentation in support of reported maintenance costs, to the extent of $5,592.

**Other Matters**

**Collaborative Agreements and Competitive Bidding**

Comment 7

AFI respectfully challenges the auditors' assessment of collaborative agreement costs. As the auditors may be aware, operation of special classes in integrated settings (SCIS) require a complement of general education students to constitute "integrated settings". These settings include early education program settings, Head Start programs. Universal pre-kindergarten settings and childcare settings. These collaborative arrangements are often memorialized in Collaborative Agreements whereunder the special education preschool (here, AFI) agrees to provide services to preschool students with disabilities and their families through a NYSED approved "4410" program, the collaboration being housed at a site operated by a community-based organization or educational program. Under the terms of such standard collaborative agreements, the community-based organization or education program agrees to cooperate to the fullest extent possible in the fulfillment of the purposes and objectives of the SCIS and to do all things necessary to that end. The terms of such collaborative agreements include "consideration" for the use and possession of a portion of the community-based organization's premises, generally considered "monthly consideration" which consists of expenses which are reasonable and allocated consistent with acceptable allocation methodologies. Again, these collaborative agreements are standard for the operation of SCIS, and the costs associated are deemed acceptable and reasonable by SED, as a matter of course. Accordingly, we respectfully request the auditors' reconsider the concerns expressed associated with such collaboration agreement payments, however mischaracterized the labeling of the payments may have been.

AFI appreciates the auditors' recommendation regarding our competitive bidding practices and has strengthened internal protocols as recommended.

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Abilities First, Inc. appreciates the team's acknowledgement of existing control activities related to accounting functions and review of work, and welcomes the opportunity to strengthen the weaknesses in policies identified by the audit team. AFI has already initiated meaningful efforts to address the auditors' attributions.

Very truly yours,

GREENBERG TRAURIG, LLP

PAM/maf
Enclosures
*ACTIVE 684876413v1*

Theresa Podagrosi
Office of the State Comptroller
Page 6

cc: Jerry Nestleroad (SED)
James Kampf (SED)
Kim Ryder (AFI)

# State Comptroller’s Comments

1. Our finding already excludes the portion of the salary that is allowable according to the RCM.
2. The time sheets provided by AFI officials for the Training, Nursing, and Speech Coordinators indicated they were working in AFI’s day treatment and school-age programs and not the Programs we reviewed.
3. Our finding already excludes the employee’s 2018 salary as Director of Preschool. AFI’s allocation methodology used in 2019 when the individual assumed responsibility as Vice President of Education was not in compliance with the requirements of the RCM and CFR Manual.
4. As stated in the report, while the expense was paid as salary and compensation, the Chief Executive Officer’s employment agreement explicitly notes the amount is for a vehicle allowance and, therefore, was not allowed according to the RCM.
5. While AFI officials state that they complied with the applicable provision of generally accepted accounting principles, the RCM does not allow for the reimbursement of future lease obligations.
6. While AFI officials state that the actual cost of the property damage was less than the insurance deductible, they did not provide documentation to support this.
7. As stated in the report, costs were not itemized on the collaboration agreement; therefore, we could not determine if any costs AFI claimed on its CFR were for non-reimbursable services, and AFI did not provide documentation to support itemization. Further, the other provider was also an SED-approved preschool special education provider, and without proper documentation, we were unable to determine if any of the expenses submitted by AFI were reimbursed by SED through the other provider’s integrated preschool special education program.

# Contributors to Report

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