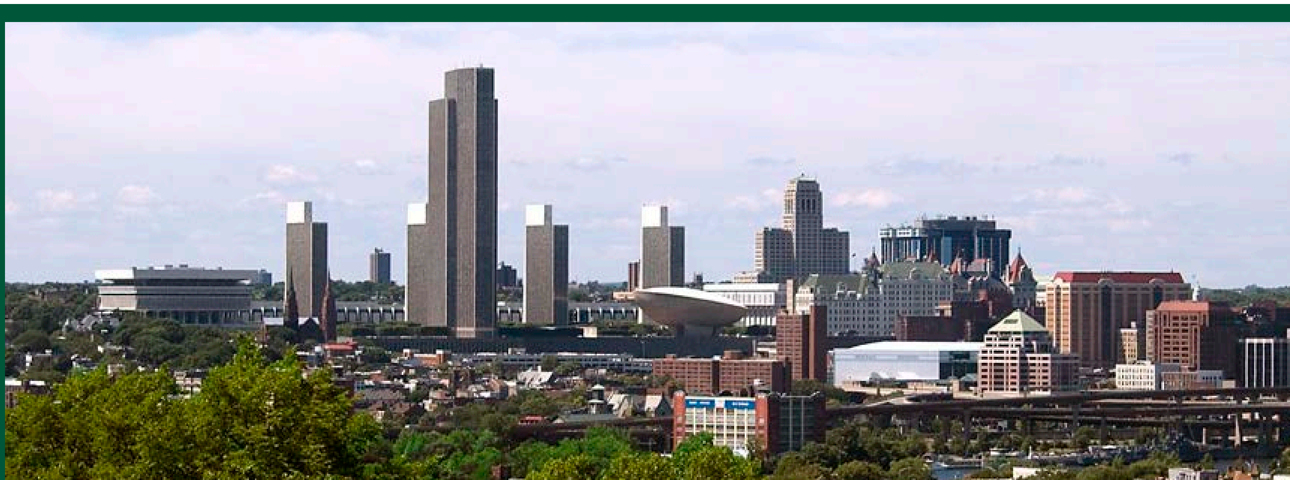
New York State Office of the State Comptroller
Thomas P. DiNapoli

Division of State Government Accountability

Compliance With the Reimbursable Cost Manual

State Education Department
Elmcrest Children's Center, Inc.



Report 2016-S-62

May 2017

Executive Summary

Purpose

To determine whether the costs reported by Elmcrest Children's Center, Inc. (Elmcrest) 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). The audit covered expenses reported on Elmcrest's CFR for the fiscal year ended June 30, 2014.

Background

Elmcrest is a not-for-profit organization located in Syracuse, New York that operates a special education integrated preschool classroom within its early education center. Elmcrest is authorized by SED to provide preschool education services to children with disabilities between the ages of three and five years. Elmcrest is reimbursed for these services through rates set by SED. These reimbursement rates are based on financial information, including costs, that Elmcrest reports to SED on its annual CFR. To be eligible for reimbursement, reported costs must comply with the RCM requirements. For the fiscal year ended June 30, 2014, Elmcrest reported approximately $2.2 million in reimbursable costs on its CFR for one rate-based preschool special education program that it operated.

Key Findings

For the fiscal year ended June 30, 2014, Elmcrest claimed $54,250 in ineligible costs for the rate-based preschool special education program that it operated. The ineligible costs included:

- $18,264 in personal service costs, which consisted of bonuses and employee fringe benefits;
- $16,578 in overstated expenses that resulted from Elmcrest understating revenue that should have been offset against program expenses;
- $12,911 in improperly allocated personal service and other than personal service costs; and
- $6,497 in other than personal service costs, which consisted of undocumented vehicle costs, ineligible consulting services costs, non-reimbursable auditing fees, and other non-reimbursable expenses.

We also determined Elmcrest did not disclose related-party transactions with two vendors on its CFR, as required.

Key Recommendations

To SED:

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

To Elmcrest:

- Ensure that costs reported on annual CFRs fully comply with SED's requirements, and communicate with SED to obtain clarification as needed.
- Ensure that related-party transactions are properly disclosed, including on the CFR.

Other Related Audits/Reports of Interest

The Arc of Orange County: Compliance With the Reimbursable Cost Manual (2015-S-45)
Center for Disability Services: Compliance With the Reimbursable Cost Manual (2015-S-40)

State of New York
Office of the State Comptroller

Division of State Government Accountability

May 24, 2017

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

Mr. Joseph Geglia
Executive Director
Elmcrest Children's Center, Inc.
960 Salt Springs Road
Syracuse, NY 13224

Dear Ms. Elia and Mr. Geglia:

The Office of the State Comptroller is committed to helping State agencies, public authorities, and local government agencies manage government resources efficiently and effectively and, by so doing, providing accountability for tax dollars spent to support government operations. The Comptroller oversees the fiscal affairs of State agencies, public authorities, and local government agencies, as well as their compliance with relevant statutes and their observance of good business practices. 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 of our audit of the expenses submitted by Elmcrest Children's Center, 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, entitled *Compliance With the Reimbursable Cost Manual*. 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,

Office of the State Comptroller
Division of State Government Accountability

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This report is also available on our website at: www.osc.state.ny.us

Background

Elmcrest Children's Center, Inc. (Elmcrest) is a not-for-profit organization located in Syracuse, New York. Elmcrest is authorized by the State Education Department (SED) to provide, among other programs, preschool special education services to children with disabilities between the ages of three and five years. Elmcrest also operates a day care center for infants, toddlers, and preschoolers as well as other related special education services. In addition, Elmcrest is a participant in the Syracuse City School District's Universal Prekindergarten (UPK) program. During our audit period, Elmcrest operated one SED-funded, rate-based preschool special education program: Preschool Integrated Special Class – over 2.5 hours per day (referred to as the Program). The Program provided services to 48 children with special education needs from Madison and Onondaga counties.

The counties that use Elmcrest's preschool special education services pay tuition to Elmcrest using reimbursement rates set by SED. The State, in turn, reimburses the counties 59.5 percent of the tuition that counties pay. SED sets the special education tuition rates based on financial information, including costs, reported by Elmcrest on the annual Consolidated Fiscal Report (CFR) that it submits to SED. Costs reported on the CFR must comply fully with the guidelines in SED's Reimbursable Cost Manual (RCM) regarding the eligibility of costs 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, 2014, Elmcrest reported approximately $2.2 million in reimbursable costs on its CFR for the Program.

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 adequately documented. For the fiscal year ended June 30, 2014, we identified $54,250 in costs that Elmcrest reported on its CFR that did not comply with SED's requirements for reimbursement. The ineligible costs included $18,264 in personal service costs, $16,578 in overstated expenses that resulted from an improper allocation of UPK revenue, $12,911 in improperly allocated expenses, and $6,497 in other than personal service (OTPS) costs. In certain instances, some of the ineligible costs were previously identified by SED, which we noted in the report.

Personal Service Costs

For the fiscal year ended June 30, 2014, we identified $18,264 in personal service costs that were not eligible for reimbursement. The ineligible costs included $16,468 in bonuses and $1,796 in fringe benefits for deferred compensation and accrued family sick leave.

Bonuses

According to the RCM, a merit award (bonus compensation) shall mean a non-recurring and non-accumulating (i.e., not included in the base salary of subsequent years) lump sum payment in excess of regularly scheduled salary which is not directly related to hours worked. A merit award may be reimbursed if it is based on merit, as measured and supported by employee performance evaluations. For the fiscal year ended June 30, 2014, we identified $16,468 in non-reimbursable bonuses ($14,804 in bonuses and $1,664 in associated fringe benefits). These bonuses were not based on merit or supported by documented employee performance evaluations, as required.

Excessive Employee Benefits

Fringe benefits include employee benefits that are required by State and federal law, such as Social Security and worker's compensation, as well as benefits that are not mandated by State or federal law, such as employer contributions to health insurance and retirement benefits. The CFR Manual states that non-qualified deferred compensation plans (per the Internal Revenue Code) are not reimbursable. Additionally, the RCM states that accrued vacation and sick leave are not reimbursable until actually paid.

We found $1,796 in non-reimbursable employee fringe benefits on Elmcrest's CFR for a non-qualified deferred compensation plan and for accrued family sick leave. Elmcrest claimed $1,313 in costs for a non-qualified deferred compensation plan for an executive, which the CFR Manual does not allow. We also found that Elmcrest reported $483 in an accrued family sick leave liability that was not paid, and as such was not reimbursable.

Misapplication of Offsetting Revenue

The RCM states that any funding received from a governmental agency or unit for a specific education program will be offset by SED against the appropriate program in the calculation of the tuition rate so that costs will not be reimbursed more than once by public funds. Elmcrest reported it received $33,156 in revenue from the city of Syracuse for services provided in lieu of tuition for UPK recipients who attended Elmcrest's program. However, if a recipient attended Elmcrest's afternoon day care program, they were required to pay an additional fee. On its CFR, Elmcrest improperly split the $33,156 in revenue evenly between the Program and its afternoon day care program (the revenue should not have been applied to the afternoon day care program). This improper revenue split resulted in an understatement of $16,578 in revenue that should have been offset against the Program's costs, creating the situation where costs were being reimbursed more than once by public funds.

Allocation Methodology and Administrative Costs

The RCM states that an expenditure that cannot be charged to a specific program must be allocated across all programs that benefit from the expenditure. Entities must use allocation methods that are fair and reasonable, and allocation percentages should be reviewed on an annual basis and adjusted, if necessary. We found Elmcrest inappropriately allocated $12,911 in shared expenses to the Program based on an incorrect application of its student slot allocation methodology ($10,398) and misclassified administration expenses ($2,513).

Incorrect Application of Allocation Methodology

For the fiscal year ended June 30, 2014, we identified $10,398 in ineligible costs that Elmcrest improperly allocated to the Program, which included $2,926 in personal service costs and $7,472 in OTPS. Elmcrest used student slot percentages to allocate shared salary, facility, and depreciation costs to the Program on its CFR (note: a slot is a seat within a program's authorized student capacity level). However, Elmcrest weighted shared student slots differently among its various programs. We determined that a disproportionate share was assigned to the student slots for the Program, which resulted in additional costs being improperly allocated to the Program. The resulting $10,398 disallowance was calculated after removing the other costs noted throughout this report that we deemed were ineligible for reimbursement.

Agency Administration Cost Misclassification

The RCM defines agency administration costs as expenses that are not directly related to a specific program but are attributable to the overall operation of an agency. The RCM prescribes that agency administration costs be allocated to all programs using the ratio value method of allocation. We found that Elmcrest incorrectly reported a total of $15,012 in agency administration costs as Program expenses, including $8,899 for an associate executive director's salary and $6,113 in OTPS costs. However, the associate director had agency-wide responsibilities and the OTPS costs were administration-related. After reclassifying these costs as agency administration and adjusting for the disallowances noted elsewhere in this report, we identified a net disallowance of $2,513 ($1,682 in personal service costs and $831 in OTPS).

Other Than Personal Service Costs

We identified $6,497 in OTPS costs that did not meet the RCM's requirements for reimbursement. This included $3,125 in undocumented vehicle costs, $1,137 in ineligible consulting services costs, $341 in ineligible auditing fees, and $1,894 in other non-reimbursable expenses such as food and entertainment for staff, executives, and the Board of Directors.

Vehicle Logs

According to the RCM, vehicle costs must be supported by individual vehicle logs that at a minimum include: the date, time of travel, to and from destinations, mileage between each destination, purpose of travel, and name of the traveler. Elmcrest reported $3,125 in vehicle costs (including gas, repairs and maintenance, insurance, and depreciation). However, Elmcrest did not maintain the required vehicle logs. Consequently, the reported costs were not reimbursable. SED previously identified a portion of these costs as ineligible for reimbursement.

Ineligible Consulting Services Costs

RCM guidelines for less-than-arm's-length (LTAL) consulting services state that such services must be reimbursed based on the owner's actual documented costs. Elmcrest entered into a consulting arrangement with a company owned by a member of its Board of Directors. However, we found Elmcrest did not have documentation showing that the amount charged for services provided was based on the owner's actual costs. As a result, $1,137 in costs paid to this consultant were ineligible for reimbursement.

Non-Allowable Auditing Expenses

The RCM states that adequate documentation for consulting services must include itemized invoices indicating: the specific services provided, dates when services were provided, number of hours provided, fee per hour, and total charged. Additionally, non-financial services provided by the financial statement auditor, within a 365-day window of required audit work, are not reimbursable. We found $341 in ineligible expenses, including $218 in undocumented auditing expenses and $123 in non-financial auditing services related to the completion of Internal Revenue Service tax forms.

Other Non-Reimbursable Expenses

According to the RCM, costs are reimbursable provided such costs are reasonable, necessary, directly related to the special education program, and properly documented. Expenses for food, gifts, donations, fundraising, and entertainment are not reimbursable. Additionally, cell phone data and text messaging charges are only reimbursable if the provider can demonstrate the business necessity. For the fiscal year ended June 30, 2014, we identified $1,894 in costs that were ineligible for reimbursement because they were not in compliance with the RCM requirements. The ineligible costs include the following:

- $1,161 in food and entertainment for staff, executives, and Board of Directors meetings;
- $389 in gifts;
- $144 in charitable contributions;
- $103 in fundraising expenses;
- $52 for non-Program and non-reimbursable messaging fees for cell phones; and
- $45 in non-Program expenses for which supporting documentation stated the expense should have been directly charged to a different program.

SED previously identified a portion of these costs as ineligible for reimbursement.

Other Matters

Unreported Less-Than-Arm's-Length Transactions

According to the RCM, providers must maintain a conflict of interest policy and fully disclose all LTAL transactions on the CFR-5 schedule. Additionally, these relationships must be disclosed in the notes to the audited financial statements. We found Elmcrest conducted business with two separate related parties who served on its Board of Directors. In both instances, Elmcrest's Board members properly disclosed the conflict of interest to Elmcrest, but Elmcrest did not report the relationship on the CFR-5 or in the notes to its audited financial statements, as required. Specifically, we found the following:

- Interest expense for a line of credit provided by First Niagara Bank. An Elmcrest Board member is a senior vice president for First Niagara.
- Costs for Program and fundraising consulting services provided by Winfield Inc., a company owned by a member of Elmcrest's Board of Directors.

We determined the line of credit Elmcrest obtained from First Niagara Bank was at the prime rate, and as such we did not deem these costs to be ineligible for reimbursement. However, Elmcrest was unable to support that the services provided by Winfield Inc. were reimbursed at the owner's costs. Consequently, we deemed this LTAL transaction ineligible for reimbursement. This ineligible cost is included in a prior section of this report (see Ineligible Consulting Services Costs).

Recommendations

To SED:

1. Review the disallowances identified by our audit and, if warranted, make the necessary adjustments to the costs reported on Elmcrest's CFR and to Elmcrest's tuition reimbursement rates.

2. Remind Elmcrest officials of the pertinent SED requirements that relate to the deficiencies we identified.

To Elmcrest:

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

4. Ensure that related-party transactions are properly disclosed, including on the CFR.

Audit Scope, Objective, and Methodology

We audited the costs Elmcrest reported on its CFR for the fiscal year ended June 30, 2014. The objective of our audit was to determine whether the reported costs were allowable, properly calculated, and adequately documented in accordance with applicable SED requirements.

To accomplish our objective, and assess internal controls related to our objective, we reviewed the RCM that applied to the year we examined, as well as the CFR Manual and its related appendices. We became familiar with Elmcrest's internal controls as they related to costs Elmcrest reported on the CFR. We also interviewed Elmcrest officials to obtain an understanding of their financial practices related to the costs reported on the CFR. We reviewed Elmcrest's CFR for the fiscal year ended June 30, 2014 as well as its audited financial statements for this period. We obtained accounting records and supporting information to assess whether a judgmental sample of costs reported by Elmcrest on the CFR were properly calculated, adequately documented, and allowable. Specifically, we reviewed costs that were considered high risk and reimbursable in limited circumstances, such as employee bonuses, vehicle, and food expenses.

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. 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 functions do not affect our ability to conduct independent audits of program performance.

Authority

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

Reporting Requirements

We provided a draft copy of this report to SED and Elmcrest 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 it. In their response, SED officials agreed with the audit recommendations and indicated the actions they will take to address them. In their response, Elmcrest officials raised concerns regarding proposed disallowances involving bonus payments, offsetting revenues, vehicle costs, and auditing expenses. Our rejoinders to Elmcrest's comments are included in the report's State Comptroller's Comments.

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

Contributors to This Report

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Ed Durocher, CIA, Audit Manager
Karen Bogucki, CGFM, Audit Supervisor
Daniel Rossi, CIA, Examiner-in-Charge
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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

Elmcrest Children's Center, Inc.
Schedule of Submitted and Disallowed Program Costs
for the Fiscal Year Ended June 30, 2014

Program Costs	Amount Per CFR	Amount Disallowed	Amount Remaining	Notes to Exhibit
Personal Service	$1,900,083	$22,872	$1,877,211	A-C,E-H
Other Than Personal Service	258,812	14,800	244,012	E-U
Total Program Costs	**$2,158,895**	**$37,672**	**$2,121,223**	
Off-setting Revenue	173,223	16,578	189,801	D
Net Expenses	**$1,985,672**	**$54,250**	**$1,931,422**	

Notes to Exhibit

The following Notes refer to specific sections of the RCM and CFR Manual that we used as a basis for our findings and recommended disallowances. We summarized the applicable sections to explain the basis for the findings and each disallowance. We provided the details supporting our recommended disallowances to Elmcrest and SED officials during the course of the audit.

A. RCM Section II.13.A(10): A merit award (or bonus compensation) shall mean a non-recurring and non-accumulating (i.e., not included in base salary of subsequent years) lump sum payment in excess of regularly scheduled salary which is not directly related to hours worked. A merit award may be reimbursed if it is based on merit as measured and supported by employee performance evaluations. In order to demonstrate that a merit award is based on merit and measured and supported by employee performance evaluations, the provider's governing entity must adopt a written employee performance evaluation policy and form that contains sufficient detail as to the criteria and methods used to determine each employee's final evaluation rating. The written employee performance evaluation policy must also describe how the final evaluation rating will directly correlate to any amount of a merit award should funds be available for such an award. In addition, merit awards: (a) are restricted to direct care titles/employees as defined by the Reimbursable Cost Manual's Appendix A-1 and those in the 100 position title code series and position title code 505 and 605 as defined by the Consolidated Fiscal Report's Appendix R; (b) will not be reimbursed if paid to subcontractors and/or independent consultants; (c) shall be subject to all aspects, constraints and cost parameters contained in the methodology; and (d) must be paid within the year awarded or no later than 2½ months after the entity's year end.
B. CFR Manual Appendix X – Adjustments to Reported Costs, Section 57.0(25): Fringe benefit expenses that are not reasonable and available to all employees including but not limited to Supplemental Executive Retirement Plans or any Non-qualified Deferred Compensation Plans subject to IRC Subsection §457(f).
C. RCM Section II.13.B(2)(a): Vacation and sick leave are reimbursable in the year actually paid and reported as a salary expense. Accrued vacation and sick leave expenses are not reimbursable until actually paid.
D. RCM Section II.44.A(2): Funding received from a governmental agency or unit for specific education programs or cost items will be offset by SED against the appropriate program costs in the calculation of tuition rates so that costs will not be reimbursed more than once by public funds.
E. RCM Section III.1.M(1): Any expenditure that cannot be charged directly to a specific program must be allocated across all programs and/or entities benefited by the expenditure.
F. RCM 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 years. Allocation percentages should be reviewed on an annual

basis and adjusted as necessary.

G. RCM Section I.9: Agency administration is defined as those expenses which are not directly related to a specific program but are attributable to the overall operation of the agency. These costs include: costs for the overall direction of the organization; costs for general recordkeeping, budget and fiscal management; costs for public relations (non-fundraising); and costs for parent agency expenditures.

H. RCM Section III.1.M(3): For CFR filers (except Office of Children and Family Services Residential Facilities), agency administration costs shall be allocated to all programs operated by the entity based on the Ratio Value Method of allocation. Agency administration costs allocated to grant cost centers shall be the lower of actual costs allowable based on the Ratio Value Method (CFR Manual, Section 15.6) or the maximum amount that can be charged based on grantor requirements.

I. RCM Section III.1.J(2): Vehicle use must be documented with individual vehicle logs that include at a minimum: the date, time of travel, to and from destinations, mileage between each, purpose of travel, and name of traveler. If the vehicle was assigned to an employee, also list the name of the employee to whom it was assigned. The annual mileage for program purposes and repairs and maintenance costs for each vehicle should be summarized and maintained.

J. RCM Section III.1.D: All purchases must be supported with invoices listing items purchased and indicating date of purchase and date of payment, as well as canceled checks. Costs must be charged directly to specific programs whenever possible. The particular program(s) must be identified on invoices or associated documents. When applicable, competitive bidding practices should be used in conformance with the Purchasing Handbook.

K. RCM Section II.14.F: Costs associated with non-audit services provided by a registered public accounting firm or any person associated with that firm, during or within 365 days of required audit work (prior to the beginning of the fiscal period being audited or after the date of the audit report issued for the audit period), are not reimbursable. Such non-audit services include: bookkeeping or other services related to the accounting records or financial statements of the audit client; financial information systems design and implementation; appraisal or valuation services, fairness opinions or contribution-in-kinds reports; actuarial services; internal audit outsourcing services; management functions or human resources; broker or dealer, investment advisor or investment banking services; legal services and expert services unrelated to the audit; and any other service that the Board of the provider does not approve, or that SED or other governing State agency does not approve as reasonable and necessary, consistent with applicable requirements and this Manual.

L. RCM Section II.22.C: Costs of food provided to any staff, including lunchroom monitors, are not reimbursable.

M. RCM Section II.30.C: Costs for food, beverages, entertainment, and other related costs for meetings, including Board meetings, are not reimbursable.

N. 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. Refer to Section II.30. Meetings and Conferences and Section II.59.

O. RCM Section II.24: Gifts of any kind are non-reimbursable.

P. RCM Section II.16: Political and charitable contributions and donations made by the program are not reimbursable.

Q. RCM Section II.23: Costs of organized fund raising (i.e., financial campaigns, endowment drives or solicitation of gifts and bequests) to raise capital, or to obtain contributions are not reimbursable. However, reasonable and necessary costs associated with the procurement and retention of donated services used for IEP mandated services either directly or indirectly, may be reimbursable as long as the program can demonstrate that cost savings exist and that there is a direct benefit to the students in the program through the use of such donated services. These costs are subject to the non-direct care cost parameter.

R. RCM Section II: 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.

S. RCM Section II.57.A: Costs incurred for telephone/cellphone service, local and long distance telephone calls, and electronic facsimiles (FAX) are reimbursable provided that they are used primarily in furtherance of the operation of the special education program. In the case of cellphone data and text messaging charges, Providers must demonstrate the business necessity for such additional cellphone features and that the cost of the plan(s) is no greater than necessary to meet the Provider's business needs. Any personal use of the devices must meet the *de minimis* fringe benefit standard as established by the IRS.

T. RCM Section I.4.B: In general, a conflict of interest exists when a person in a position of trust has a competing professional or personal interest. The existence of a conflict of interest does not mean that an unethical or improper act has occurred or will occur. However, care must be taken to ensure that such conflicts do not impair the employee's ability to perform his or her duties objectively and act in the best interest of the entity. Each provider must adopt a written conflict of interest policy that clearly sets forth the procedures to be followed in instances where a member of the governing entity of the provider (for example, the provider's Board or person in a management position) have personal or business interests that may be advanced by an action of the Board, including a provision that such member may not participate in any decision to approve any transaction where such conflicting interests may be advanced. The policy must also include a requirement and process for identifying and fully disclosing all LTAL relationships and transactions on an ongoing basis as well as on the CFR. The policy should be reviewed and discussed with the provider's attorneys and auditors prior to its adoption.

U. RCM Section I.4.F.7: All LTAL transactions will be reimbursed using actual documented costs of the owner or vendor. Invoices presented to the approved special education provider by the LTAL party do not constitute "actual costs." Actual costs are those the LTAL party incurs and it is expected upon audit or review, that the LTAL party will produce evidence of its costs. Commissioner's designee's written approval is required to reimburse at a level other than actual costs of the owner or vendor.

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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May 12, 2017

Ms. Andrea Inman
Audit Director
Office of the State Comptroller
Division of State Government Accountability
110 State Street – 11th Floor
Albany, NY 12236

Dear Ms. Inman:

The following is the New York State Education Department's (Department) response to the draft audit report, 2016-S-62, Compliance with the Reimbursable Cost Manual: Elmcrest Children's Center, Inc. (Elmcrest).

Recommendation 1: Review the disallowances identified by our audit and, if warranted, make the necessary adjustments to the costs reported on Elmcrest's CFR and to Elmcrest's tuition reimbursement rates.

We agree with this recommendation; however, SED will review further the Elmcrest and the OSC application of the slot allocation methodology for allocating costs between the integrated program and after school daycare program. After giving additional consideration to this finding, 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 Elmcrest 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 the Elmcrest 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
Suzanne Bolling

Agency Comments - Elmcrest Children's Center, Inc.

elmcrest
Building on the promise of children and families.

May 10, 2017

Mr. Edward J. Durocher, CIA
Audit Manager
Office of the State Comptroller
110 State Street, 11th Floor
Albany, NY 12236-0001

Dear Mr. Durocher:

In response to your draft audit report dated April 2017 reviewing our Consolidated Fiscal Report for the year ended June 30, 2014 we respectfully submit the following facts and comments for inclusion in your final audit report.

For several years our SED-funded preschool integrated special education program has been over the SED calculated total cost screen. This is due primarily to a trend of 0% colas and rising expenses including health insurance, workers compensation insurance, utilities and liability insurance.

The Tuition Rate Analysis prepared by SED for our program for the year audited shows screened out costs of $150,457. Our total cost screen for the year ended June 30, 2014 was $1,826,825 and the expenses totaled $1,977,282, leaving $150,457 unreimbursed. This is a key point for SED and other readers to understand. The audit report asserts $54,250 in ineligible costs, a balance well below the $150,457 Elmcrest invested of their own funds to properly educate and prepare for kindergarten the preschool children enrolled in our special needs integrated program.

* Comment 1

In addition, the following responses relate to the specific audit findings in the audit report.

Personal Service Costs:

- Bonuses – Whenever Elmcrest can reward employees for their hard work we thank them for their many contributions with a small year-end bonus. As the SED rates have been flat with no colas for years the most prudent way to support our employees financially is through a one-time bonus rather than adding to their base salary. Based on Agency-wide performance for the year ended June 30, 2014 a flat $300 bonus was given to each full time staff member employed for the full fiscal year. The majority of our Early Ed employees earned between $8 - $11/hour and greatly appreciated the year end bonus and special recognition.

* Comment 2

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* See State Comptroller's Comments, page 20.

Misapplication of Offsetting Revenue:

- Splitting the UPK Revenue in half between the morning program and the afternoon program was how we were instructed by our SED Representative to report the $33,156 in revenue. Recruiting typical children to integrate within our special education program is one of our biggest ongoing struggles. UPK revenue gives parents financial incentive to enroll their children in the program. The additional amount parents pay out of pocket to have their children stay in the afternoon after UPK is over was also split evenly between the morning special education program and the afternoon day care program. We were being consistent with both sources of offsetting revenue.

* Comment 3

Other Than Personal Service Costs:

- **Vehicle Logs** -We do maintain vehicle logs for all vehicles except the maintenance & food service vehicles which are used for Agency wide purposes. Given the nature of the use of these vehicles making frequent stops at each program on our campus to deliver food and supplies, plow snow, etc. a vehicle log does not make sense and provides no basis for allocating costs appropriately.

* Comment 4

- **Non-Allowable Auditing Expenses** - The $341 disallowed for audit services includes audit services and the 990 and CHAR500 preparation for the Agency. These services provided by our auditors are Agency wide expenses that should be allocated to the program and are wise financial investments to ensure tax return accuracy.

* Comment 5

We wish to thank the Staff of the Office of the State Comptroller for their courteous and professional work during the four month process of reviewing our Consolidated Fiscal Report for the fiscal year ended June 30, 2014.

Sincerely,

Terri Tulowiecki

Terri Tulowiecki

Associate Executive Director of Financial Operations

State Comptroller's Comments

1. The methodology our auditors used to identify non-allowable costs is different from the methodology SED used to screen out costs. To the point, our audit testing was based on a review of source documentation for a sample of expenses reported on the CFR. In contrast, SED's cost screen methodology involved ensuring that the provider's costs did not exceed certain thresholds, known as cost screens.
2. The RCM is very clear regarding the reimbursement of bonus compensation (merit awards). Specifically, a bonus may be reimbursed if it is based on merit as measured and supported by employee performance evaluations. Elmcrest officials did not provide any evidence that the bonus payments were based on merit or supported by documented employee performance evaluations. Therefore, we maintain that the $16,468 in bonus payments is not reimbursable.
3. Elmcrest was not able to provide documentation to support its claim that SED instructed it to split the $33,156 in revenue in half between the two programs. Further, SED officials were not aware of any such instructions being provided. As stated on page 7 of our report, according to the RCM, funding received from a governmental agency for a specific education program should be offset against the corresponding program's expenses so that costs will not be reimbursed more than once by public funds. Elmcrest received $33,156 in revenue from the city of Syracuse for services provided to UPK recipients who attended Elmcrest's program. Elmcrest split this revenue evenly between the Program and its afternoon day care program, even though UPK services were only offered during the Program's hours of operation. As such, the UPK revenue should have been entirely offset against Program costs. Consequently, Elmcrest understated Program revenues by $16,578, which created a situation where costs were reimbursed more than once by public funds.
4. The RCM requires individual vehicle logs to document vehicle usage. There are no exceptions to this requirement. Elmcrest did not maintain logs for the vehicles in question, and as such we maintain that the $3,125 in vehicle costs is not reimbursable.
5. As stated on page 8 of our report, Elmcrest did not have the RCM-required supporting documentation for $218 in auditing expenses. In addition, Elmcrest's financial statement auditors provided $123 in non-financial audit services (i.e., tax preparation services) within 365 days of required audit work, which is not reimbursable per the RCM. Therefore, we maintain that the $341 in costs is not reimbursable.