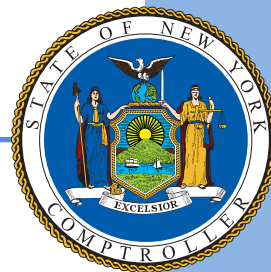


# 2016 Annual Report on Preschool Special Education Audit Initiative

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OFFICE OF THE NEW YORK STATE COMPTROLLER

Thomas P. DiNapoli, State Comptroller



JANUARY 2017

# Message from the Comptroller

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January 2017

Special education programs fulfill a great need across New York State, providing our youngest citizens with disabilities a quality learning experience that addresses their individual differences and needs. While many private special education providers use public funds conscientiously and in accordance with State rules, there are others that abuse the system and misuse the funding they receive from the State and local governments, resulting in taxpayers paying more than they should for these vital programs.

Over the last decade, my office has found a persistent pattern of mismanagement, waste and even fraud by numerous private providers of preschool special education services. Our audits have uncovered inaccurate and inappropriate self-reported program costs, as well as ineffective program monitoring and oversight. As a result, children needing special education services have been shortchanged by those private providers who have inappropriately used public funds.

The State Legislature responded to these reports of abuse by passing legislation requiring my office to audit the expenses submitted by every provider of preschool special education services to the State Education Department (SED) at least once and to report annually on our findings to the Governor and the Legislature. This is the third such annual report.

To improve the oversight and management of this essential public program, we've coordinated our audit efforts with the SED, the New York City Department of Education, the New York State Association of Counties, and individual counties themselves. We also provide training to county officials and private providers to explain the importance of this initiative and to discuss fraud prevention and detection techniques, the findings of our audits, and the need for strong internal controls.

This year's audits show that there's been an improvement in cost reporting by preschool special education providers to the SED. As we continue monitoring the costs for preschool special education services, my office will continue to promote best practices and to emphasize the importance of critical internal controls and responsible external oversight.

Thomas P. DiNapoli  
State Comptroller



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# Executive Summary

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State Education Law makes school districts responsible for the provision of services to students with disabilities, including preschool students, and authorizes them to contract for necessary educational services with private providers. Currently, the New York State Education Department (SED) reports that over 80,000 preschool students with disabilities receive services in New York at an annual cost of about \$1.4 billion to the State and its local governments.

Unlike in other states, preschool special education services in New York are predominantly provided by private providers (both for-profit and not-for-profit) rather than the school districts themselves. These providers must be approved by SED, which annually develops reimbursement rates for programs operated by approved providers based on actual costs reported to SED. These rates are used to compensate providers for eligible costs, which must be in compliance with comprehensive guidelines promulgated by SED. There are currently over 300 approved private preschool special education providers in the State.

For more than a decade, the Office of the State Comptroller (OSC) has conducted dozens of audits of expenses submitted by special education providers to SED, which focused on providers' compliance with SED cost-reporting guidelines and the accuracy and appropriateness of self-reported program costs. These audits identified patterns of providers seeking reimbursement for unsupported expenditures, expenses claimed for other programs, personal expenses included with program expenses, no-show jobs, and increased costs associated with less-than-arm's-length transactions. OSC concluded that stopping fraudulent, wasteful, and abusive practices by providers required a more comprehensive approach.

In June 2012, Comptroller DiNapoli announced a new special education audit initiative, which involved a broader, sector-wide perspective as well as multiple simultaneous individual audits, and proposed legislation to improve the oversight of public funding for preschool special education services. OSC also conducted an audit of SED's fiscal and program oversight of special education providers and issued an audit report in December 2012.

As a result, Chapter 545 of the Laws of 2013 was signed into law on December 18, 2013. The law requires the State Comptroller to audit the expenses reported to SED by every program provider of special education services for preschool children with disabilities at least once, subject to the funding made available by the Legislature for such purpose. The law also requires the Comptroller to report annually to the Governor and the Legislature regarding the audits conducted during the preceding 12 months.

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As of December 2016, OSC has completed and issued 89 audits of expenses submitted to SED by preschool and/or school age special education providers over the last decade, including 26 issued in 2016. These audits have cumulatively identified over \$57 million in recommended disallowances, or 5.5 percent of the total claimed expenses of over \$1 billion. In one instance, OSC coordinated with the New York State Office of the Attorney General and the New York State Department of Taxation and Finance in 2016 on an audit-related investigation that resulted in a settlement of over \$4.3 million.

While the audits completed in 2016 continued to find issues akin to those found in the audits completed in previous years, auditors found that there has been an improvement in cost reporting by the preschool special education providers to SED.

On October 1, 2016, Section 200.18 of the Regulations of the Commissioner of Education was amended to make clear that SED shall review OSC's final audit reports, which shall be used to establish tuition rates based on audit to the extent the Commissioner determines that the audit findings and recommended disallowances are warranted and consistent with applicable laws, regulations and guidelines.

# Overview

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## Background

New York State's longstanding commitment to providing special education services to students with disabilities predates federal mandates. Enacted in 1975, the federal Education for All Handicapped Children Act (now the Individuals with Disabilities Education Act, or IDEA, as amended) requires that all students with disabilities be provided with a free appropriate public education in the least restrictive environment possible. Prior to the IDEA, parents of children with disabilities in New York State had to petition the Family Court and their county of residence to receive services under the Family Court Act of 1962.

In 1989, legislative changes were enacted to add a new Section 4410 to the State Education Law pertaining to preschool children. As a result, school districts became responsible for services to preschool students with disabilities aged three and four. Because of the previous involvement of the counties and the Family Court in determining approved services, counties are required to continue to pay for special education services for preschoolers while receiving partial reimbursement from the State.

The New York State Education Department (SED) reports that about 80,000 preschool students with disabilities receive services throughout the State annually from over 300 approved providers. Eligible students may receive related services only, services of a Special Education Itinerant Teacher (SEIT), or be placed in a special class program for either a half day or a full day, including integrated programs for students without disabilities when appropriate. New York's system allows for the provision of related and SEIT services within general education preschool and/or day care environments as well as in the child's home.

The cost of these services is substantial. SED reports that about \$1.4 billion is spent annually by the State and its local governments on services for preschool special education students aged three and four. Unlike in other states, preschool special education services in New York are predominantly provided by private providers (both for-profit and not-for-profit) rather than public school districts. These providers must be approved by SED to deliver special education services to children. SED annually develops rates for preschool special education programs (programs) operated by approved providers based on actual costs reported to SED. These rates are used to reimburse providers for eligible costs, which must be in compliance with comprehensive instructions and guidelines set forth in the Consolidated Fiscal Reporting and Claiming Manual (CFR) and the Reimbursable Cost Manual (RCM).

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Over the past decade, the Office of the State Comptroller (OSC) has conducted dozens of audits of expenses submitted to SED by preschool special education providers, which focused on compliance with SED cost-reporting guidelines and the accuracy and appropriateness of provider-reported program costs. These audits identified patterns of providers seeking reimbursement for unsupported expenditures, expenses claimed for other programs, personal expenses included with program expenses, no-show jobs, and increased costs associated with less-than-arm's-length transactions. OSC concluded that stopping fraudulent, wasteful and abusive practices by these providers required a more comprehensive approach.

Toward this end, Comptroller DiNapoli launched a special education audit initiative in June 2012 that would encompass audits drawn from a broader, sector-wide perspective as well as multiple simultaneous individual audits, and involve better coordination with SED and the New York City Department of Education (DOE), input from various interested parties, use of data analysis and risk analysis, and use of fraud and forensic auditing techniques. As an added measure, in tandem with the initiative, Comptroller DiNapoli also proposed legislation to improve oversight of public funding of preschool special education services.

## **Chapter 545 Legislation**

Comptroller DiNapoli's proposal, known as Chapter 545 of the Laws of 2013, was signed into law on December 18, 2013. Under the law, the State Comptroller is required to audit the expenses reported to SED by every program provider of special education services for preschool children with disabilities at least once, "within such funds as are made available for such purpose." The statute requires the State Comptroller to "inform and advise the governor and the legislature in December of each year regarding its audits of expenses reported to the department by program providers of special education services for preschool children with disabilities conducted during the preceding 12 months and regarding any other pertinent information the comptroller deems appropriate." This report fulfills the statutory reporting requirement under Chapter 545 for 2016.

Chapter 545 also directed SED to conduct a comprehensive study of alternative systems of reimbursement methodologies and monitoring protocols for the tuition and maintenance components of preschool special education services. SED submitted its study on December 18, 2014. Based on the study's recommendations, Chapter 56 of the Laws of 2015 amended Section 4410 of the Education Law by adding a new provision as follows: "Notwithstanding any other provision of law, rule or regulation to the contrary, on or before the two thousand sixteen—two thousand seventeen school year and thereafter, to be phased-in over no more than four years from such starting year, the commissioner, subject to the approval of the director of the budget, shall establish regional tuition



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rates for special education itinerant services based on average actual costs in accordance with a methodology established pursuant to subdivision four of section forty-four hundred five of this article.” SED has also enacted amendments to the Regulations of the Commissioner of Education that strengthened other aspects of the preschool special education program. These are discussed later in this report.

## **OSC Initiative Activities**

As required by Section 4410-c of the Education Law, OSC developed a risk assessment process to prioritize the preschool special education audits to be undertaken in accordance with the initiative. This includes performing ongoing analysis of the data reported to SED by providers on their annual Consolidated Fiscal Reports (CFRs) to identify high-risk indicators. These indicators are used to assist auditors with the identification of high-risk expenses and the development of a comprehensive audit plan for the initiative.

OSC developed standard audit protocols and a specialized audit template to ensure consistency in the preschool special education audits. OSC also established protocols to refer findings of fraud, abuse or other conduct constituting a crime identified during an audit to OSC’s internal investigations unit as well as to external agencies with appropriate legal jurisdiction. OSC incorporated these protocols into specialized training provided to all staff engaged in the audit initiative.

OSC has continued to provide training for preschool special education providers that addresses fraud detection and prevention. As part of this training, providers have been given information on the OSC audit process, beginning with the issuance of an engagement letter through the release of a final report. The training also addresses the State’s expectations with respect to documentation of reimbursable costs. During 2016, OSC provided two training sessions to 185 special education provider staff. OSC has collaborated with SED, the counties, the New York City DOE, the New York State Association of Counties and other external groups to provide regular updates on OSC training and audit activities.

To facilitate this collaboration, OSC has established a dedicated electronic mailbox to communicate with and provide guidance and information to external stakeholders. The mailbox is used to communicate with preschool special education providers on matters related to the OSC Training Initiative. These include notification of dates and locations of available training sessions, training enrollment, and answers to any training-related matters.

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The mailbox is also used as a platform by OSC, SED, the counties, and the New York City DOE to coordinate efforts in auditing preschool special education services and programs. In 2016, OSC used the mailbox to send an informational email to all special education providers and county officials regarding SED's proposed amendment to Section 200.18 of the Regulations of the Commissioner, discussed later in this report.

SED has supported measures to remove disincentives for municipalities to audit preschool special education programs by increasing the share of overpayments that may be recovered by a municipality conducting a fiscal audit of such services or programs for which it bears fiscal responsibility, and proportionally reducing the State's share of such disallowed funds. Section 4410 of the Education Law includes provisions which authorize a municipality to retain 100 percent of recoveries identified by its audits.

The New York City DOE and the counties of Monroe, Onondaga and Suffolk conduct their own fiscal audits of local preschool special education programs delivering services within their jurisdictions, completing approximately 27 audits to date.

## **Collaboration with Other State Agencies**

OSC collaborated with the New York State Office of the Attorney General and the New York State Department of Taxation and Finance in the investigation of a preschool special education provider whose claimed expenses had previously been audited by OSC. The OSC audit (completed in September of 2015) identified over \$1.8 million in recommended disallowances related to excessive executive compensation, lobbying and legal fees, and errors in accounting methodologies. The subsequent investigation identified a complex leasing arrangement that resulted in inflated claims for rent reimbursement for the provider's preschool education program. Related tax issues were also identified. The provider and other parties have agreed to pay the State over \$4.3 million to resolve the matter.

# Audit Findings

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In 2016, OSC completed 26 audits of expenses submitted to SED by preschool special education providers. These audits have cumulatively identified about \$5.5 million in recommended disallowances, or nearly 3 percent of the total claimed expenses of almost \$188 million for the audit period. There are currently 22 additional audits in progress, including two that have been completed but not yet issued.

Disallowed expenses range from claimed costs for services provided directly to children to administrative functions. In the past, OSC's audits of expenses submitted to SED by certain special education providers identified widespread mismanagement and blatant misuse of public funds intended for the education of children with disabilities, as well as outright fraud. The audits completed in 2016 show there is some improvement in cost reporting by the preschool special education providers to SED. However, although the dollar amount of the findings has decreased, the number of findings in certain categories continues to be of concern.

The 2016 audit findings can be summarized as follows:

**Personal Service-Related Findings** – OSC audits completed and issued in 2016 identified almost \$3 million of unsupported or ineligible payroll-related expenses:

- **Unsupported or ineligible payroll expenses** – SED requires providers to base employee compensation on approved and documented payrolls, which are supported by employee time and attendance records for all employees. Also, Section 200.9 of the Regulations of the Commissioner of Education (Regulations) states that providers shall maintain adequate records to document direct and/or indirect service hours provided as well as time spent on all other activities related to each student served. In addition, the RCM requires salaries of employees who perform tasks for more than one program to be allocated among all programs for which they work. Furthermore, entities must maintain appropriate documentation reflecting the hours used in this allocation. Eighteen out of 26 audits found issues with the maintenance of payroll and time distribution documentation as required by the RCM. Nine of the 18 audits identified payroll costs from other programs charged to the preschool programs. The number of payroll-related problems reported in 2016 is slightly higher than those reported in prior years.
- **Unsupported bonuses** – SED requires that salary bonuses be based on merit and supported by performance evaluations to be eligible for reimbursement. Eleven of the 26 audits found evidence of claimed bonuses that were not in compliance with the RCM, a decrease from the number reported in 2015.

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**Other Than Personal Services (OTPS)-Related Findings** – 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 properly documented. In addition, expenses of a personal nature are not reimbursable. OSC audits completed and issued in 2016 identified almost \$2.5 million in unsupported or ineligible OTPS-related expenses:

- **Unsupported/Ineligible Costs** – In nearly all of the audited programs (22 out of 26), there were findings of ineligible expenses, which were either not program-related or not supported by adequate documentation. The findings increased in dollar value from about \$477,000 in 2015 to about \$1.1 million reported this year. This includes \$138,000 for claimed costs related to staff food and entertainment, which was a decrease in such claimed costs from prior periods (\$760,000 in 2014 and \$165,595 in 2015).
- **Penalties, Interest, Fines and Late Fees** – The RCM expressly states that fines, penalties, late fees, and certain forms of interest are not reimbursable. The RCM further states that costs resulting from violations of, or failure by, the entity to comply with federal, State, and/or local laws and regulations are not reimbursable. Findings in this cost category were not included in the 2014 or 2015 report. In 2016, 11 of the 26 audits noted recommended disallowances for non-reimbursable penalties, interest, fines and late fees.
- **Vehicle-Related Expenses** – SED allows for the reimbursement of vehicle costs as long as vehicle usage is program-related and documented in logs, which include dates, times, purposes, destinations, mileage and names of persons using the vehicles. More than a third of the audits (10 out of 26) identified recommended disallowances of vehicle-related expenses, which were inadequately documented or otherwise ineligible for reimbursement—a slight decrease from the number of problems reported in 2015.
- **Consultant Services** – The RCM provides extensive guidance on the use of consultants, the proper claiming of costs for their services, and related supporting documentation requirements. The RCM requires that the selection of consultant services must be done at a minimum of every five years through a competitive bid process. In addition, the consultant services cannot be used for services that could have been performed by a properly certified school officer or an employee who possesses the necessary technical skills. Almost a third of the audits (7 out of 26) noted recommended disallowances for consultant services. The 2016 audits found a decrease in the number of problems reported in 2015, but an increase in the dollar amount of the findings from about \$414,000 to about \$695,000 or almost 13 percent of total disallowed claimed expenses.

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### **Expenses Claimed from Other Programs and Incorrect Allocation of Costs –**

SED guidelines require that any expenditure that cannot be charged directly to a specific program be allocated across all programs and/or entities that benefit from the expenditure (e.g., general maintenance and overhead expenses). The RCM requires providers to maintain documentation of the methodologies used to allocate costs to the various programs which they operate. In addition to the personal service costs previously noted, almost half of the audits completed and issued in 2016 (12 out of 26) identified problems related to the allocation of OTPS costs among programs and/or the inappropriate claiming of expenses from other programs.

SED also requires providers to correctly classify costs as either direct care costs (those associated with the provision of instruction and related services to students) and non-direct care costs (those attributable to the general administration of a program and/or the operation and maintenance of a program's facilities). Six of the 26 audits identified issues related to allocation of costs between direct and non-direct care, a slight increase from the number of problems noted in 2015.

### **Errors in Account Methodologies Used for Depreciation, Amortization and**

**Accruals –** SED guidelines permit reimbursement of the depreciation of capital assets and the amortization of financing costs over the useful life of the assets or financing. Seven out of 26 audits found the inappropriate expensing of such costs—a slight increase from the number of problems noted in 2015.

### **Undisclosed Less-Than-Arm's-Length (LTAL) Transactions –**

SED requires special education providers to disclose all less-than-arm's-length (LTAL) transactions in their CFRs and in the notes to their audited financial statements. In brief, a LTAL relationship exists when there are related parties and one party can control or significantly influence the business decisions of another party due to the nature of their personal relationships (e.g., spouses who conduct business with each other). Disclosure of such relationships is necessary to help ensure the propriety of costs for reimbursement purposes. Similar to last year, 3 out of 26 audits identified LTAL transactions which were not disclosed as required. Additionally, two audits identified significant problems with reported costs related to LTAL business transactions even though the relationship was disclosed on the CFRs.

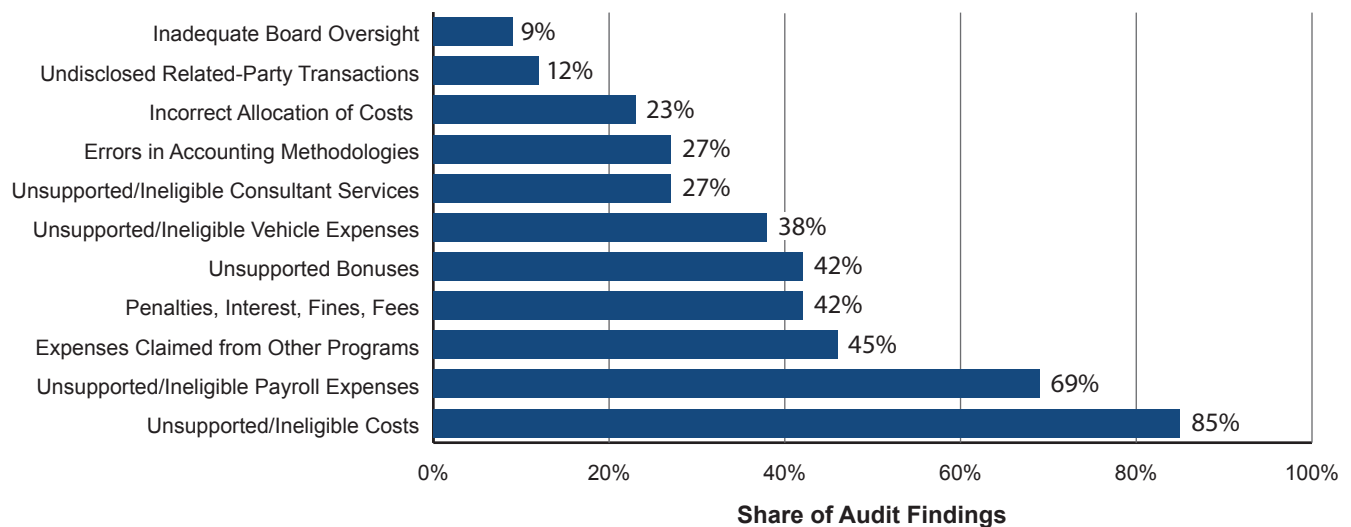
### **Oversight by Boards of Directors and Systems of Internal Controls –**

When providers are overseen by boards of directors, board members are subject to certain standards, including meeting fiduciary responsibilities, remaining independent, meeting at least twice annually, maintaining accurate board minutes, complying with conflict of interest policies and filing annual disclosure statements. In 22 of the 26 audits conducted in 2016, the providers were overseen by boards of directors. OSC audits reported that two of those boards of directors did not provide adequate oversight and/or establish adequate systems of internal controls.

**Lack of Due Diligence by Certified Public Accountants** – As part of the CFR submission process, each provider is required to have an independent certified public accountant (CPA) express an opinion on its financial statements and certify that its CFR is prepared in accordance with SED guidelines. The purpose of the certification is to ensure that the CFR data is reported consistently and can be relied upon for the rate-setting process. OSC audits completed in 2016 continue to find numerous errors in costs reported in CFRs that can be attributed to the lack of due diligence by CPAs hired by special education providers. Examples include instances of claimed expenses for other programs included with preschool special education costs reported on CFRs; LTAL transactions; errors in allocation methodologies; and errors in accounting methodologies used for depreciation, amortization, and accruals. Therefore, OSC will continue to closely monitor the role of CPAs in the CFR submission process.

The following graph includes some of the more common findings and their corresponding rates of occurrence, as identified in our reports in 2016.

### Patterns of Inappropriate Claimed Expenses for Special Education Services in New York State



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## Special Education Program Audits Completed and Issued in 2016

**Aim High Children's Services (Aim High) (2015-S-62)** is a not-for-profit organization located in Brooklyn, New York, that provides special education services to children with disabilities from birth to five years of age. For the three-year period ended June 30, 2014, Aim High reported approximately \$9.8 million in reimbursable costs for its special education programs. The OSC audit recommended disallowances of \$616,906 in reported costs that did not comply with SED's requirements for reimbursement, including:

- \$501,085 in payments to seven other schools for mainstream educational services because Aim High could not provide the required supporting documentation (including the cost allocation methodology used) for the payments in question;
- \$75,256 for ineligible costs associated with non-audit services provided by a registered CPA firm within 365 days of audit work; and
- \$22,139 in personal service costs that were over-allocated to the SED programs.

**Baker Victory Services (Baker Victory) (2015-S-57)** is a not-for-profit organization located in Lackawanna, New York, that provides a range of community-based programs, including preschool special education services to children with disabilities who are between the ages of three and five years. For the fiscal year ended June 30, 2014, Baker Victory reported about \$6.9 million in reimbursable costs for its special education programs. The OSC audit recommended disallowances of \$155,303 in reported costs that did not comply with SED's requirements for reimbursement, including:

- \$53,053 for public relations and advertising costs that were either not supported, not allowed, or not directly related to the programs;
- \$46,526 for staff bonuses and fringe benefits that were not based on merit;
- \$22,925 in salary expenses for an employee whose title and job description were not applicable to the programs; and
- \$14,849 in ineligible costs such as charitable donations, membership dues, training expenses and food, entertainment and gifts provided to staff and board members.

In addition, the OSC audit found that improvements are needed in Baker Victory's internal control structure to help ensure that allocated program costs reported on annual CFRs fully comply with SED's requirements.

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**Benchmark Family Services, Inc. (Benchmark) (2016-S-47)** is a for-profit organization located in Watertown, New York, that provides special education services to children with disabilities from birth to five years of age. For the fiscal year ended June 30, 2013, Benchmark reported \$669,689 in reimbursable costs for its special education programs. The OSC audit recommended disallowances of \$18,012 in OTPS costs that did not comply with SED's requirements for reimbursement.

**Bornhava (2016-S-23)** is a not-for-profit organization located in Buffalo, New York, that provides special education services to children with disabilities from birth to five years of age. For the fiscal year ended June 30, 2014, Bornhava reported about \$1.8 million in reimbursable costs for its special education programs. The OSC audit recommended disallowances of \$14,237 in reported costs that did not comply with SED's requirements for reimbursement, including \$9,055 for ineligible salary and fringe benefit expenses and \$5,182 in OTPS costs that were not allowable.

**Center for Disability Services (CFDS) (2015-S-40)** is a not-for-profit organization located in Albany, New York, that provides a range of services and programs to children with disabilities who are between the ages of three and five years. For the calendar year ended December 31, 2013, CFDS reported about \$4.8 million in reimbursable costs for its special education programs. The OSC audit recommended disallowances of \$81,581 in reported costs that did not comply with SED's requirements for reimbursement, including:

- \$56,298 for ineligible employee bonuses and associated fringe benefits; and
- \$16,627 for costs that were not eligible for reimbursement, including vehicle costs, gifts and food, and costs unrelated to the program.

**Crossroads Center for Children (Crossroads) (2015-S-87)** is a not-for-profit organization based in Schenectady, New York, that provides preschool special education services to children with disabilities who are between the ages of three and five years in five upstate counties. For the fiscal year ended June 30, 2014, Crossroads reported about \$1.27 million in reimbursable costs for its special education programs. The OSC audit recommended disallowances of \$14,297 in reported costs that did not comply with SED's requirements for reimbursement, including: \$11,111 for iPads, software, laptops and various materials purchased with grant funds received by Crossroads; and \$2,281 to a CPA firm for ineligible non-audit services.

**Early Education Center, Inc. (Center) (2015-S-96)** is a for-profit organization located in Highland, New York, that offers a range of services and programs to children with disabilities who are between the ages of three and five years from 11 school districts located in three counties in the Hudson Valley region of New York. For the fiscal year ended June 30, 2014, the Center reported about



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\$2.4 million in reimbursable costs for the programs. The OSC audit recommended disallowances of \$11,508 in reported costs that did not comply with SED's requirements for reimbursement, including \$9,937 for two vehicles that had missing or incomplete vehicle logs.

**Easter Seals New York (Easter Seals NY) (2015-S-27)** is a not-for-profit organization that provides a range of community-based programs and special education services throughout New York State. Easter Seals NY provides preschool special education services to children with disabilities who are between the ages of three and five years at their Bronx, Monticello, Port Jervis and Valhalla locations. For the three-year period ended December 31, 2013, Easter Seals NY reported over \$27.6 million in reimbursable costs for its special education programs. The OSC audit recommended disallowances of \$688,543 in reported costs that did not comply with SED's requirements for reimbursement, including:

- \$546,263 in personal service costs that exceeded the staffing ratios approved by SED;
- \$110,206 in parent agency administration fees for services provided by Easter Seals New Hampshire that included executive compensation above the allowed regional median salary, bonus payments to non-direct care staff, non-reimbursable food and gifts and other unsupported charges or duplicative charges; and
- \$19,714 for gifts to employees and other individuals.

**Fred S. Keller School (FSK) (2015-S-98)** is a not-for-profit organization located in Palisades and Yonkers, New York, that provides special education services to children with disabilities between the ages of three and five years. For the fiscal year ended June 30, 2014, FSK reported about \$21 million in reimbursable costs for its special education programs. The OSC audit recommended disallowances of \$455,117 in reported costs that did not comply with SED's requirements for reimbursement, including:

- \$224,430 for unnecessary consultant costs to train employees;
- \$78,474 for non-program-related consultant costs;
- \$41,388 for consultant costs that were insufficiently documented;
- \$35,988 for insufficiently documented vehicle costs;
- \$29,059 in non-reimbursable purchases that included expenses for company barbecues, parties, entertainment, gift certificates, food, staff clothing, gifts, and flowers; and
- \$24,249 in undocumented credit card purchases.

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The OSC audit also questioned the propriety of certain actions involving FSK's Board of Directors that pertained to related-party business transactions. For example, three of FSK's four-member Board had significant business transactions with FSK. The OSC auditors concluded that improvements in the Board of Directors' conduct are needed to ensure the financial and programmatic integrity of FSK's programs in the future.

**Gingerbread Learning Center, Inc. (Gingerbread) (2014-S-79)** is a not-for-profit organization located in Staten Island, New York, that provides a range of community-based programs and special education services to children between the ages of three to five years. For the three-year period ended June 30, 2013, Gingerbread reported about \$12.2 million in reimbursable costs for its special education programs. The OSC audit recommended disallowances of \$942,998 in reported costs that did not comply with SED's requirements for reimbursement, including:

- \$246,777 in fringe benefit expenses that were unsupported, ineligible and did not comply with the RCM's guidelines;
- \$219,459 in over-allocated compensation costs associated with shared employees from its Early Intervention and Evaluation programs;
- \$185,629 in expenses that were not adequately documented, including \$46,615 in school supplies, \$41,601 in depreciation and \$21,575 in Costco purchases;
- \$160,206 in contributions made to a 401(k) plan for the Executive Director and Program Director that were in excess of contribution rates made to other Gingerbread employees;
- \$142,093 in employee bonuses, including \$75,000 in accrued bonuses that were never paid to employees;
- \$58,064 in expenses with no supporting documentation; and
- \$54,009 in expenses that were not eligible for reimbursement such as food purchases, liquor store purchases, staff holiday parties and gifts.

**Hebrew Institute for the Deaf and Exceptional Children (Hebrew Institute) (2015-S-67)** is a not-for-profit organization located in Brooklyn, New York, that provides special education services to children with disabilities from birth to five years of age. For the three-year period ended June 30, 2014, Hebrew Institute reported about \$11 million in reimbursable costs for its special education programs. The OSC audit recommended disallowances of \$774,122 in reported costs that did not comply with SED's requirements for reimbursement, including:

- \$194,438 in lump sum bonuses that did not comply with the RCM's requirements;

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- \$132,846 in over-allocated compensation costs for 24 shared employees;
  - \$132,377 in excessive executive compensation;
  - \$121,660 in undocumented and/or insufficiently documented expenses, including \$56,568 in compensation paid to eight employees, \$22,024 in checks written out to the Executive Director, \$10,000 to a consultant, and \$5,728 in petty cash disbursements;
  - \$108,639 in non-mandated fringe benefit contributions that did not comply with the RCM's requirements;
  - \$53,533 in ineligible expenses, including \$13,641 for staff food, \$12,514 in referral fees to employees, and \$11,244 in legal fees not related to the SED cost-based programs; and
  - \$30,629 in expenses for vehicles used by the Executive Director that were not supported by usage logs.

**Helping Hands School (Helping Hands) (2015-S-90)** is a not-for-profit organization located in Clifton Park, New York. Helping Hands offers a range of services and programs for children with disabilities from three to five years of age from 20 school districts located in four counties in upstate New York. For the fiscal year ended June 30, 2014, Helping Hands reported about \$2.5 million in reimbursable costs for its special education programs. The OSC audit recommended a disallowance of \$26 in reported OTPS costs that did not comply with SED's requirements for reimbursement.

**HTA of New York, Inc. (HTA) (2016-S-36)** is a for-profit organization located in Westchester County, New York, that provides special education services to children with disabilities from birth to five years of age. For the fiscal year ended June 30, 2014, HTA reported about \$2 million in reimbursable costs for its special education programs. The OSC audit recommended disallowances of \$28,952 in reported costs that did not comply with SED's requirements for reimbursement, including \$22,207 in OTPS costs and \$6,745 in personal service costs.

**Jawonio, Inc. (Jawonio) (2015-S-49)** is a not-for-profit facility located in Rockland County, New York, that provides preschool special education services to children with disabilities who are between the ages of three and five years. For the calendar year ended December 31, 2014, Jawonio reported over \$3.5 million in reimbursable costs for its special education programs. The OSC audit recommended disallowances of \$26,975 in reported costs that did not comply with SED's requirements for reimbursement, including \$24,611 in excess personal service costs paid to senior executives and \$2,364 in OTPS costs.

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**JCC of Mid-Westchester (JCC) (2016-S-21)** is a not-for-profit organization located in Scarsdale, New York, that provides special education services to children with disabilities from birth to five years of age. For the three-year period ended June 30, 2014, JCC reported about \$5 million in reimbursable costs for its special education programs. The OSC audit recommended disallowances of \$90,900 in reported costs that did not comply with SED's requirements for reimbursement, including:

- \$20,883 in expenses that were related to the JCC gymnastics program;
- \$17,738 in personal service costs for teacher aides in excess of approved staffing ratios;
- \$14,196 in non-allowable depreciation costs; and
- \$10,172 in OTPS administration expenses that were incorrectly allocated.

**Jowonio School (Jowonio) (2016-S-48)** is a not-for-profit organization located in Syracuse, New York, that provides special education services to children with disabilities from birth to five years of age. For the three fiscal years ended June 30, 2014, Jowonio reported about \$7 million in reimbursable costs for its special education programs. The OSC audit recommended disallowances of \$118,110 in reported costs that did not comply with SED's requirements for reimbursement, including:

- \$98,572 in ineligible employee bonuses; and
- \$19,538 in OTPS costs, which included \$16,656 for insufficiently documented vehicle costs.

**Kidz Therapy Services, PLLC (Kidz Therapy) (2015-S-63)** is a for-profit organization located in Garden City, New York, that provides special education services to children between the ages of three and five years. For the three fiscal years ended June 30, 2014, Kidz Therapy reported approximately \$4.77 million in reimbursable costs for its SEIT program. The OSC audit recommended disallowances of \$249,850 in reported costs that did not comply with SED's requirements for reimbursement, including:

- \$164,004 in salaries and related fringe benefits for six teachers that were over-allocated to the program;
- \$37,041 in fringe benefit expenses that did not comply with the RCM;
- \$17,300 in employee bonuses for staff who did not serve in direct care titles;
- \$3,211 in payments to a limited liability company when no services were provided; and
- \$2,153 in privately owned vehicle expenses for the Executive Director and the CFO.

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**League for the Handicapped (LFH) (2015-S-89)** is a not-for-profit organization located in Springville, New York. LFH offers a range of services and programs to children with disabilities from birth through eight years of age from 35 school districts located in three counties in western New York. For the fiscal year ended June 30, 2014, LFH reported about \$2.9 million in reimbursable costs for its special education programs. The OSC audit recommended disallowances of \$4,354 in reported costs that did not comply with SED's requirements for reimbursement, including \$2,159 in non-reimbursable vehicle costs and \$1,080 for contracted services for children not in the program.

**New York Center for Child Development, Inc. (NYCCD) (2015-S-101)** is a not-for-profit organization located in New York City that provides special education services to children with disabilities from birth to five years of age. For the three fiscal years ended June 30, 2014, NYCCD reported about \$24 million in reimbursable costs for its special education programs. The OSC audit recommended disallowances of \$776,901 in reported costs that did not comply with SED's requirements for reimbursement, including:

- \$308,905 for inadequately documented costs for two consultants;
- \$254,268 in over-allocated staff salaries for three employees;
- \$65,705 for incorrectly allocating costs from other programs for repairs and maintenance, cellphone, and supplies and materials;
- \$38,923 in non-program personal service expenses, including \$20,618 paid to the executive assistant and the executive director, and \$18,305 in compensation paid to a NYCCD employee who also worked for the executive director's for-profit entity; and
- \$21,591 in unsupported and non-program related travel expenses.

In addition, the audit recommended a disallowance of \$50,175 in non-allowable rent expenses. NYCCD's executive director owns a 50 percent share of the building leased by NYCCD for its SED programs, which is an LTAL transaction. The OSC auditors found that NYCCD did not comply with the RCM's guidelines to calculate the executive director's actual cost for the LTAL space.

**Rochester Childfirst Network (RCN) (2016-S-15)** is a not-for-profit organization located in Rochester, New York, that provides special education services to children with disabilities from birth to five years of age. For the fiscal year ended June 30, 2014, RCN reported \$752,438 in reimbursable costs for its special education programs. The OSC audit recommended disallowances of \$13,201 in reported costs that did not comply with SED's requirements for reimbursement, including \$6,159 in personal service costs and \$7,042 in OTPS costs.

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**Susan E. Wagner Preschool (Wagner) (2015-S-100)** a.k.a. the Northeast Bronx Day Care Center Inc. is a not-for-profit organization located in the Bronx, New York, that provides special education services to children with disabilities from birth to five years of age. For the three year period ended June 30, 2014, Wagner reported about \$17.1 million in reimbursable costs for its special education programs. The OSC audit recommended disallowances of \$140,902 in reported costs that did not comply with SED's requirements for reimbursement, including:

- \$81,370 for real estate taxes paid in excess of lease agreements;
- \$39,709 in unsupported and/or ineligible compensation costs for six employees; and
- \$18,650 in consultant costs that were inadequately documented.

**The Alcott School (Alcott) (2015-S-97)** is a not-for-profit organization located in Scarsdale, New York, that provides preschool special education services to children with disabilities between three and five years of age. For the fiscal year ended June 30, 2014, Alcott reported about \$4.3 million in reimbursable costs for its special education programs. The OSC audit recommended disallowances of \$55,969 in reported costs that did not comply with SED's requirements for reimbursement, including \$49,874 in unsupported payroll expenses for five employees, \$2,568 in excess compensation for employees and \$3,527 in OTPS costs that were not adequately documented or not eligible for reimbursement.

**The Arc of Orange County (Arc Orange) (2015-S-45)** is a not-for-profit organization that provides a range of community-based programs and special education services throughout Orange County, New York. Arc Orange offers preschool special education services to children with disabilities who are between the ages of three and five years. For the calendar year ended December 31, 2013, Arc Orange reported over \$5.5 million in reimbursable costs for its special education programs. The OSC audit recommended disallowances of \$81,107 in reported costs that did not comply with SED's requirements for reimbursement, including:

- \$69,310 in excessive severance payments for one employee;
- \$17,720 for tuition paid on behalf of a non-preschool employee; and
- \$5,413 in food, gift cards, and other ineligible expenses.

**The Arc of Ulster-Greene (Ulster-Greene) (2015-S-60)** is a not-for-profit organization located in Kingston, New York, that provides a range of services and programs to children with disabilities between the ages of three and five years from 10 school districts located in Ulster, Greene and Delaware counties. For the calendar year ended December 31, 2014, Ulster-Green reported about \$2.6 million in reimbursable costs for its special education programs. The OSC audit recommended disallowances of \$995 in reported costs that did not comply with SED's requirements for reimbursement.

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**The Child Development Council, Inc. (TCDC) (2016-S-22)** is a not-for-profit organization located in Johnson City, New York, that provides special education services to children with disabilities from birth to five years of age. For the fiscal year ended June 30, 2014, TCDC reported about \$1.8 million in reimbursable costs for its special education programs. The OSC audit recommended disallowances of \$16,699 in reported OTPS costs that did not comply with SED's requirements for reimbursement, including \$6,294 in costs that were over-allocated from other programs and \$5,185 in costs that were undocumented or ineligible for reimbursement.

The OSC audit also identified \$1,412 in undocumented expenses that were paid to companies owned by members of TCDC's Board of Directors and were not disclosed on the CFR as required.

**Westchester Community Opportunity Program, Inc. (WestCOP) (2016-S-33)** is a not-for-profit organization located in Westchester County, New York, that provides special education services to children with disabilities from birth to five years of age. For the year ended June 30, 2013, WestCOP reported about \$2 million in reimbursable costs for its special education programs. The OSC audit recommended disallowances of \$87,017 in reported costs that did not comply with SED's requirements for reimbursement, including:

- \$44,262 in lease expenses that were not properly allocated to the program;
- \$22,766 in non-program-related expenses; and
- \$10,525 for staff costs in excess of approved staffing ratios.

The OSC audit also determined WestCOP did not disclose related-party transactions with three vendors on its CFR, as required.

# Impact of Audits: Agency Responses and Actions Taken

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## State Education Department

SED has reviewed OSC's recommended disallowances, made adjustments to reimbursable costs, recalculated tuition rates as appropriate and recovered any overpayments resulting from such recalculations. SED continues to take actions to strengthen the fiscal oversight and accountability of preschool special education providers, including the following:

**Special Education Financial Advisory Workgroup** – The New York State Board of Regents created a Special Education Financial Advisory Workgroup to allow all interested stakeholders to provide input on the current tuition rate-setting structure for special education services and programs, and to discuss recommendations to maximize the efficient and effective use of State and local resources. SED reports that in May and June of 2015, a subcommittee of this workgroup met to discuss changes to the Special Education Itinerant Services (SEIS) rate-setting methodology, which were adopted for the 2015-16 and 2016-17 school years. SED's objectives for the 2015-16 and 2016-17 SEIS rates were: (1) to account for a reasonable student absentee factor to be included in rates under a fee-for-service reimbursement methodology; (2) to make adjustments to reimbursable costs to better reflect appropriate costs of providing SEIS as referenced in SED's methodology study (released in December 2014); and (3) to begin the phase-in of regional rates over a four-year period as directed in Chapter 56 of the Laws of 2015.

**Enhanced Program Monitoring and Program Reapproval Process** – SED has developed a comprehensive approach to improve its oversight of existing preschool special education providers, including developing a revised monitoring review protocol, conducting at least 50 onsite preschool program reviews annually, using program reviews as the basis for official program reapproval determinations, and initiating a cyclical schedule for the review and reapproval of all existing private preschool special education providers. According to information provided by SED to OSC, SED staff had completed 238 reapproval reviews of preschool special education providers at the conclusion of the 2015-16 school year.

**Required CFR Training** – Beginning with the submission of CFRs for the 2012-13 school year, SED encouraged all individuals signing the CFR certification statements (namely Executive Directors and CPAs) either to attend an interagency CFR training offered annually at one of six locations across the State or to complete an online CFR training course. SED is tracking and verifying the individuals who have completed the required training. SED intends to make this training a requirement as part of the new application process. According to information provided by SED, 286 Executive Directors, administrative staff and CPAs affiliated with providers have participated in CFR training conducted by SED through November 2016, with over 400 individuals registered to attend the remaining training sessions offered in December 2016.



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**Revised SED Regulations** – In 2016, SED amended the Regulations of the Commissioner relating to preschool providers to clarify, consistent with State law, the locations where SEIS may be provided and to ensure preschool students enrolled in special classes receive the related services in their Individualized Education Program (a written statement of the educational program designed to meet a child's individual needs) in conjunction with their special class programs. In addition, the regulations enhanced program standards for the instruction of preschool students with disabilities relating to: instruction toward the Prekindergarten Foundation for the Common Core; literacy instruction; progress monitoring; engagement of parents; make up of missed services; and use of positive behavioral supports.

Section 200.18 of the Regulations of the Commissioner was amended to make clear that SED shall review final audit reports, which shall be used to establish tuition rates based on audit to the extent the Commissioner determines that the audit findings and recommended disallowances contained therein are warranted and consistent with applicable laws, regulations and guidelines.

Further, after consideration of the final audit by the Commissioner, tuition rates based on audit shall then be established by the Commissioner and become final after certification by the Director of the Budget.

# Conclusion

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As New York continues to strengthen its oversight of preschool special education services and programs, State policy makers must continue their efforts to encourage all stakeholders to commit long-term to making this important sector of the State's education system work more efficiently and effectively. Accordingly, the Office of the State Comptroller will carry on its efforts to promote best practices and to emphasize the importance of critical internal controls and responsible external oversight. The Office will continue its partnership with other State agencies to identify fraud, waste and abuse in programs designed to assist New Yorkers.

# Appendix A

## 2016 OSC Special Education Program Audits

| Provider/Audit Name                                    | County      | Audited Program Costs Reported on CFR | Number of Years in Scope | Total Disallowance  |
|--|-------------|---------------------------------------|--------------------------|---------------------|
| Aim High Children's Services                           | Kings       | \$9,755,107                           | 3                        | \$616,906           |
| Baker Victory Services                                 | Erie        | \$6,876,784                           | 1                        | \$155,303           |
| Benchmark Family Services, Inc.                        | Jefferson   | \$669,689                             | 1                        | \$18,012            |
| Bornhava   | Erie        | \$1,809,554                           | 1                        | \$14,237            |
| Center for Disability Services                         | Albany      | \$4,770,552                           | 1                        | \$81,581            |
| Crossroads Center for Children                         | Schenectady | \$1,274,168                           | 1                        | \$14,297            |
| Early Education Center, Inc.                           | Ulster      | \$2,399,671                           | 1                        | \$11,508            |
| Easter Seals New York                                  | Multi       | \$27,553,262                          | 3                        | \$688,543           |
| Fred S. Keller School                                  | Westchester | \$21,257,416                          | 3                        | \$455,117           |
| Gingerbread Learning Center, Inc.                      | Richmond    | \$12,207,558                          | 3                        | \$942,998           |
| Hebrew Institute for the Deaf and Exceptional Children | Kings       | \$11,030,694                          | 3                        | \$774,122           |
| Helping Hands School                                   | Saratoga    | \$2,466,062                           | 1                        | \$26                |
| HTA of New York, Inc.                                  | Westchester | \$2,658,964                           | 1                        | \$28,952            |
| Jawonio, Inc.  | Rockland    | \$3,518,992                           | 1                        | \$26,975            |
| JCC of Mid-Westchester                                 | Westchester | \$5,390,172                           | 3                        | \$90,900            |
| Jowonio School   | Onondaga    | \$7,657,344                           | 3                        | \$118,110           |
| Kidz Therapy Services, PLLC                            | Nassau      | \$4,773,358                           | 3                        | \$249,850           |
| League for the Handicapped                             | Erie        | \$2,885,257                           | 1                        | \$4,354             |
| New York Center for Child Development, Inc.            | New York    | \$24,488,806                          | 3                        | \$776,901           |
| Rochester Childfirst Network                           | Monroe      | \$752,438                             | 1                        | \$13,201            |
| Susan E. Wagner Preschool                              | Kings       | \$17,105,607                          | 3                        | \$140,902           |
| The Alcott School                                      | Westchester | \$4,360,862                           | 1                        | \$55,969            |
| The Arc of Orange County                               | Orange      | \$5,523,866                           | 1                        | \$81,107            |
| The Arc of Ulster-Green                                | Ulster      | \$2,598,052                           | 1                        | \$995               |
| The Child Development Council, Inc.                    | Broome      | \$1,842,329                           | 1                        | \$16,699            |
| Westchester Community Opportunity Program, Inc.        | Westchester | \$2,059,359                           | 1                        | \$87,017            |
| Additional Audits Completed in 2016, Not Issued        |             | \$147,909,935                         |                          | \$6,013,365         |
| <b>Total</b>   |             | <b>\$335,595,858</b>                  |                          | <b>\$11,477,947</b> |

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