



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 Leake and Watts Services, Inc.



Executive Summary

Purpose

To determine whether the costs reported by Leake and Watts Services, Inc. (Leake and Watts) 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 the expenses reported on Leake and Watts' CFR for the fiscal year ended June 30, 2015.

Background

Leake and Watts (which, in 2018, changed its name to Rising Ground) is an SED-approved, not-for-profit special education provider located in Westchester County, New York. Leake and Watts provides preschool special education services to children with learning disabilities who are between three and five years of age. Leake and Watts is reimbursed for preschool special education services through rates set by SED. The reimbursement rates are based on financial information, including costs, that Leake and Watts reports to SED on its annual CFR. To be eligible for reimbursement, reported costs must comply with RCM requirements. For the fiscal year ended June 30, 2015, Leake and Watts reported approximately \$6 million in reimbursable costs on its CFR for the seven rate-based preschool special education Programs (Programs) that it operated.

Key Findings

For the fiscal year ended June 30, 2015, we identified \$228,071 in ineligible costs that Leake and Watts reported on its CFR for the Programs. The ineligible costs included:

- \$162,753 in personal service costs, which consisted of \$158,044 in salaries and fringe benefits for staff working outside the Programs, \$2,747 in executive compensation that exceeded the regional median compensation level, and \$1,962 in costs for seven administrative staff whose compensation exceeded one full-time equivalent; and
- \$65,318 in other than personal service costs, which consisted of \$53,960 in insufficiently documented expenses and \$11,358 in ineligible expenses.

Key Recommendations

To SED:

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

To Leake and Watts:

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

Other Related Audit/Report of Interest

[The Network for Children's Speech, Occupational & Physical Therapy, LLC: Compliance With the Reimbursable Cost Manual \(2017-S-79\)](#)

**State of New York
Office of the State Comptroller**

Division of State Government Accountability

December 27, 2018

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

Mr. Alan Mucatel
Executive Director
Rising Ground
463 Hawthorne Avenue
Yonkers, NY 10705

Dear Ms. Elia and Mr. Mucatel:

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

This audit's results and recommendations are resources for you to use in effectively managing your operations and in meeting the expectations of taxpayers. If you have any questions about this 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

Leake and Watts Services, Inc. (Leake and Watts) is a not-for-profit organization located in Westchester County, New York.¹ Leake and Watts is authorized by the State Education Department (SED) to provide, among other programs, preschool special education services to children with learning disabilities who are between three and five years of age. During our audit period, Leake and Watts operated seven rate-based preschool special education programs: two Preschool Special Class programs – over 2.5 hours per day; two Preschool Special Class programs – 2.5 hours per day; two Preschool Integrated Special Class programs – over 2.5 hours per day; and one Preschool Integrated Special Class program – 2.5 hours per day (collectively referred to as the Programs). The Programs served 291 children with special education needs from Westchester County and New York City. Leake and Watts is managed by a board of directors.

Any county that uses Leake and Watts' preschool special education services pays tuition to Leake and Watts using reimbursement rates set by SED. The State, in turn, reimburses the counties 59.5 percent of the tuition that the counties pay. SED sets the special education tuition rates based on financial information, including costs, reported by Leake and Watts 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, 2015, Leake and Watts reported approximately \$6 million in reimbursable costs for the Programs on its CFR.

¹ In 2018, subsequent to the period covered by our audit, Leake and Watts changed its name to Rising Ground.

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, 2015, we identified \$228,071 in costs that did not comply with the RCM's requirements for reimbursement. The ineligible costs included \$162,753 in personal service costs and \$65,318 in other than personal service (OTPS) costs (see the Exhibit at the end of this report).

Personal Service Costs

For the fiscal year ended June 30, 2015, Leake and Watts reported a total of \$162,753 in personal service costs on its CFR that were not allowable under SED's requirements.

Direct Care Personal Service Costs

The RCM stipulates that, to be eligible for reimbursement, costs must be directly related to the Programs and sufficiently documented. Additionally, compensation costs must be supported by employee time records prepared during the time period for which the employee was paid. We determined that Leake and Watts reported \$158,044 in excess personal service costs (\$121,318 in salary and \$36,726 in associated fringe benefits) for nine staff who either did not work in the Programs (3) or whose time records did not support hours worked and charged to the Programs (6).

Median Salary Adjustment

The RCM states that compensation for an entity's Executive Director will be directly compared to the regional median compensation for comparable job titles of public schools. Reimbursement of employee compensation for this job title shall not exceed the median compensation paid to comparable personnel in public schools for similar work and hours of employment in that region. We determined Leake and Watts compensated its Executive Director \$35,207 in excess of the regional median compensation level for this position, of which \$2,747 was charged to the Programs. SED previously identified these costs as ineligible for reimbursement.

Non-Direct Personal Service Costs

According to the RCM, compensation beyond one full-time equivalent (FTE) for non-direct care staff, owners, or related parties is non-reimbursable. We determined that Leake and Watts' reported compensation for seven staff exceeded 1.0 FTE. As a result, Leake and Watts reported \$1,962 in excess non-direct care personal service costs (\$1,506 in salary and \$456 in associated fringe benefits) that were ineligible for reimbursement.

Other Than Personal Service Costs

For the fiscal year ended June 30, 2015, Leake and Watts reported a total of \$65,318 in OTPS costs on its CFR that were not allowable under SED's requirements.

Insufficiently Documented Costs

According to the RCM, costs must be sufficiently documented. Additionally, all payments to consultants must be supported by itemized invoices that indicate the specific services actually provided and, for each service, the date(s), number of hours provided, fee per hour, and total amount charged. Furthermore, costs associated with retainers for legal, accounting, or consulting services are not reimbursable unless the fees represent payment for actual documented services rendered. We identified \$53,960 in costs reported by Leake and Watts on its CFR that were not sufficiently documented and thus were ineligible for reimbursement as follows:

- \$27,125 in depreciation and insurance expenses incorrectly charged as direct expenses to the Programs; lacking documentation to show the costs were directly related to the Programs, the expenses should have been charged as administrative expenses and allocated across all of Leake and Watts' programs;
- \$23,660 in costs that were insufficiently documented;
- \$1,755 in consulting fees that were not appropriately itemized; and
- \$1,420 in retainer fees for public relations consulting costs.

Other Ineligible Costs

According to the RCM, costs must be reasonable, necessary, and directly related to the special education programs. The RCM also lists other specific conditions under which costs are not reimbursable. For instance, costs associated with entertainment of officers or employees; food for staff; gifts of any kind; student recruitment; clothing for staff; and fines and penalties for violation of federal, State, and/or local laws and regulations are not reimbursable. Furthermore, the RCM requires that items with a unit cost of \$5,000 or more and an estimated useful life of two years or more should not be reported as expenses but, instead, must be capitalized. We identified \$11,358 in costs that were ineligible for reimbursement because they were not in compliance with these RCM requirements. The ineligible costs consisted of:

- \$7,234 in costs that should have been capitalized;
- \$852 in food and beverages for staff or for activities not related to the Programs;
- \$822 in costs associated with another reporting period;
- \$750 in fines/penalties for violations;
- \$653 in entertainment for staff;
- \$588 in gifts;
- \$320 in student recruitment; and
- \$139 for staff uniforms.

Recommendations

To SED:

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

To Leake and Watts:

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

Audit Scope, Objective, and Methodology

We audited the costs that Leake and Watts reported on its CFR for the fiscal year ended June 30, 2015. 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, we reviewed the RCM that applied to the year we examined as well as the CFR Manual and its related appendices. We also evaluated the internal controls over the costs claimed on, and the schedules prepared in support of, the CFR submitted to SED. We interviewed Leake and Watts' personnel to obtain an understanding of the practices for reporting costs on the CFR. We reviewed Leake and Watts' CFR for the fiscal year ended June 30, 2015 and relevant financial records for the audit period. We reviewed accounting records and supporting information to assess whether certain costs claimed by Leake and Watts on the CFR that were considered high risk and reimbursable in limited circumstances (such as salaries, consulting, and food transactions) were allowable, properly calculated, and documented.

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 Leake and Watts officials for their review and formal comment. We considered the comments offered in preparing this report. In SED's response, officials agreed with the audit recommendations and indicated the actions they will take to address them. SED's response is included at the end of this report. Leake and Watts officials did not provide formal comments on the findings and recommendations included in the draft audit report. Instead, Leake and Watts sent an email stating that they do not agree with the draft audit report and directed us to their August 2018 response to our preliminary audit findings as their basis for disagreement. We considered Leake and Watts' preliminary audit response in preparing this report and we concluded that officials failed to provide documentation to support their position. As such, we maintain that the \$228,071 in costs charged on the CFR were not in compliance with the RCM's requirements and were, therefore, not reimbursable.

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

Contributors to This Report

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Vision

A team of accountability experts respected for providing information that decision makers value.

Mission

To improve government operations by conducting independent audits, reviews, and evaluations of New York State and New York City taxpayer-financed programs.

Exhibit

Leake and Watts Services, Inc.
Schedule of Submitted and Disallowed Program Costs
for the Fiscal Year Ended June 30, 2015

Program Costs	Amount per CFR	Amount Disallowed	Amount Remaining	Notes to Exhibit
Personal Services	\$5,153,198	\$162,753	\$4,990,445	B, F, G, S-U
Other Than Personal Services	907,646	65,318	842,328	A-E, H-R, V-X
Total Program Costs	\$6,060,844	\$228,071	\$5,832,773	

Notes to Exhibit

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

- A. RCM Section I.9: Agency administration is defined as those expenses that are not directly related to a specific program but are attributable to the overall operation of the agency.
- B. RCM Section II: Costs are considered for reimbursement if they are reasonable, necessary, directly related to the special education program, and sufficiently documented.
- C. RCM Section II.2.B: Administrative costs may include depreciation on assets related to administration, and administrative purchases of services.
- D. RCM Section II.3.A: Advertising costs for the purpose of recruiting students into programs or soliciting fundraising monies or donations are not reimbursable and remain non-allowable in the calculation of tuition rates.
- E. RCM Section II.11: Clothing expenses for staff, such as uniforms for custodians or bus drivers, even if required by school policy, are not reimbursable.
- F. RCM Section II.13.A.(4)(a): Compensation for an entity's staff whose function is that of Executive Director will be directly compared to the regional median compensation for comparable administration job titles of public school districts. Reimbursement of employee compensation for this job title shall not exceed the median compensation paid to comparable personnel in public schools for similar work and hours of employment in the region in which the entity is located.
- G. RCM Section II.13.A.(4)(b): For non-direct care staff, compensation of up to 1.0 FTE for that individual will be considered in the calculation of the portion of 1.0 FTE reimbursable in the tuition rates.
- H. RCM Section II.14.B: Costs associated with retainers for legal, accounting, or consulting services are not reimbursable unless the fee represents payment for actual documented reimbursable services rendered.
- I. RCM Section II.17.A.(1): Items having a unit cost of \$5,000 or more and an estimated useful life of two years or more must be capitalized. Group purchases of similar items or separate purchases of similar items in the same fiscal year totaling \$5,000 or more should be treated as a single unit purchase.
- J. RCM Section II.20.A: Costs incurred for entertainment of officers or employees, for activities not related to the program, or for any related items such as meals, transportation, and gratuities, are not reimbursable.
- K. RCM Section II.20.B: All personal expenses, such as gift certificates to staff and vendors, are not reimbursable.
- L. RCM Section II.21: Costs resulting from violations of, or failure by, the entity to comply with federal, State, and/or local laws and regulations, are not reimbursable.
- M. RCM Section II.22.C: Costs of food provided to staff are not reimbursable.
- N. RCM Section II.24: Gifts of any kind are non-reimbursable.
- O. RCM Section II.30: Conferences must be directly related to the education program or

to the administration of the program. Programs shall be required upon audit to provide brochures, agendas, or other literature that verifies attendance and documents the purpose of the conference.

- P. RCM Section II.30.C: Costs for food, beverages, entertainment, and other related costs for meetings, including Board meetings, are not reimbursable.
- Q. RCM Section II.30.E: Costs of conferences attended by administrative staff are reimbursable provided that the purpose of the conference is to improve or demonstrate new administrative techniques or concepts and the criteria above (Section II.30) are met.
- R. RCM Section II.59.B: Out-of-state travel should be severely restricted and should be on an exception basis only. Out-of-state travel costs are reimbursable to the extent they are critical to the success of the program and are for services or training that cannot be obtained in State.
- S. RCM Section III.1: Section 200.9(d) of the Commissioner's Regulations requires entities operating approved programs to retain all pertinent accounting, allocation, and enrollment/attendance records supporting reported data directly or indirectly related to the establishment of tuition rates for seven years following the end of each reporting year. Costs will not be reimbursable upon field audit without appropriate written documentation of costs.
- T. RCM Section III.1.A: Compensation costs must be on approved, documented payrolls. Payroll must be supported by employee time records prepared during, not after, the time period for which the employee was paid. Employee time sheets must be signed by the employee and a supervisor and must be completed at least monthly.
- U. RCM Section III.1.B: Actual hours of service are the preferred statistical basis upon which to allocate salaries and fringe benefits for shared staff who work on multiple programs. Entities must maintain appropriate documentation reflecting the hours used in this allocation. Acceptable documentation may include payroll records and time studies. Documentation for all statistical methods must be retained for seven years.
- V. RCM Section III.1.C.(2): All payments for consultant services must be supported by itemized invoices that indicate the specific services actually provided and, for each service, the date(s), number of hours provided, fee per hour, and total amount charged.
- W. RCM Section III.1.D: All purchases must be supported with canceled checks and invoices listing the items purchased, date of purchase, and date of payment.
- X. RCM Section III.1.M.(3): For CFR filers, agency administration costs shall be allocated to all programs operated by the entity based on the Ratio Value Method of allocation.

Agency Comments - State Education Department



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

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November 30, 2018

Ms. Andrea Inman
Audit Director
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Division of State Government Accountability
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Albany, NY 12236

Dear Ms. Inman:

The following is the New York State Education Department's (SED) response to the draft audit report, 2017-S-73, Compliance with the Reimbursable Cost Manual: Leake and Watts Services, Inc. (Leake and Watts).

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

We agree with this recommendation. SED will review the recommended disallowances as noted in the report and make adjustments to the reported costs to recover any overpayments, as appropriate, by recalculating tuition rates. SED will further review the recommended disallowances for the integrated classroom staff and also determine whether the revenues associated with these expenses should be adjusted accordingly.

Recommendation 2: Remind Leake and Watts 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 Leake and Watts 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, 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. This training is a requirement for preschool special education providers upon approval and reapproval.

If you have any questions regarding this response, please contact Harold Matott, Director of the SED Rate Setting Unit at (518) 474-3227.

Yours truly,

 Sharon Cates-Williams
 Deputy Commissioner

c: Karla Ravida
 Christopher Suriano
 Suzanne Bolling
 James Kampf