New York State Comptroller
THOMAS P. DiNAPOLI

# Buffalo Hearing & Speech Center, Inc.: Compliance With the Reimbursable Cost Manual

## State Education Department

Report 2020-S-20 | **May 2021**

Spotlight on Education

# Audit Highlights

## Objective

To determine whether the costs and revenues reported by Buffalo Hearing & Speech Center, Inc. (Center) 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 the Center's 2017 and 2018 CFRs for the fiscal year ended June 30, 2018, as well as Medicaid revenues reported for the three fiscal years ended June 30, 2018.

## About the Program

The Center is an SED-approved special education provider located in Erie County. Among other programs, the Center provides preschool special education services to children with disabilities who are between three and five years of age in Western New York. The Center is reimbursed for these services through rates set by SED. The reimbursement rates are based on financial information, including costs, that the Center reports to SED on its annual CFRs. To be eligible for reimbursement, reported costs must comply with RCM requirements. For the fiscal year ended June 30, 2018, the Center reported approximately $9 million in reimbursable costs on its CFR for the Preschool Special Class – over 2.5 hours per day, Preschool Integrated Special Class – over 2.5 hours per day, and Preschool Integrated Special Class – 2.5 hours per day (collectively referred to as the Programs) that it operated.

## Key Findings

For the fiscal year ended June 30, 2018, we identified $272,526 in ineligible costs reported by the Center on its CFRs for the Programs. The ineligible costs included:

- $226,577 in personal service costs consisting of $208,482 in unsupported costs; $6,620 in excess staffing; $5,656 in bonuses; $5,259 in auto allowances; and $560 in personal service-driven allocations.
- $45,949 in other than personal service costs consisting of $27,436 in unsupported costs; $4,356 in incorrectly allocated costs; and $14,157 in other non-reimbursable costs such as gifts, food for staff, and costs not relevant to the Programs.

For the three fiscal years ended June 30, 2018, SED failed to offset $307,735 in Medicaid fee-for-service revenue received by the Center when calculating the Center's tuition rate. As a result, the Center received $216,451 in excess public funding reimbursements.

## Key Recommendations

**To SED:**

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

**To the Center:**

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

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

May 27, 2021

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

Joseph Cozzo
President/Chief Executive Officer
Buffalo Hearing & Speech Center, Inc.
50 East North Street
Buffalo, NY 14120

Dear Dr. Rosa and Mr. Cozzo:

The Office of the State Comptroller is committed to helping State agencies, public authorities, and local government agencies manage their resources efficiently and effectively. By so doing, it provides accountability for the tax dollars spent to support government operations. The Comptroller oversees the fiscal affairs of State agencies, public authorities, and local government agencies, as well as their compliance with relevant statutes and their observance of good business practices. This fiscal oversight is accomplished, in part, through our audits, which identify opportunities for improving operations. Audits can also identify strategies for reducing costs and strengthening controls that are intended to safeguard assets.

Following is a report, entitled *Compliance With the Reimbursable Cost Manual*, of our audit of the costs submitted by Buffalo Hearing & Speech 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. This audit was performed pursuant to the State Comptroller's authority under Article V, Section 1 of the State Constitution; Article II, Section 8 of the State Finance Law; and Section 4410-c of the Education Law.

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

Respectfully submitted,

*Division of State Government Accountability*

# Contents

# Glossary of Terms

| Term | Description | Identifier |
|---|---|---|
| Center | Buffalo Hearing & Speech Center, Inc. | *Service Provider* |
| CEO | Chief Executive Officer | *Key Term* |
| CFR | Consolidated Fiscal Report | *Key Term* |
| CFR Manual | Consolidated Fiscal Reporting and Claiming Manual | *Policy* |
| FTE | Full-time equivalent | *Key Term* |
| OTPS | Other than personal service | *Key Term* |
| Programs | Preschool Special Education Classes and Preschool Integrated Special Classes | *Key Term* |
| RCM | Reimbursable Cost Manual | *Policy* |
| SED | State Education Department | *Auditee* |

# Background

Buffalo Hearing & Speech Center, Inc. (Center) is a not-for-profit organization with administrative offices located in Erie County and operations throughout Western New York. The Center is authorized by the State Education Department (SED) to provide, among other programs, preschool special education services to children with disabilities who are between three and five years of age. During our audit period, the Center operated three rate-based preschool education programs: Preschool Special Class – over 2.5 hours per day, Preschool Integrated Special Class – over 2.5 hours per day, and Preschool Integrated Special Class – 2.5 hours per day (collectively referred to as the Programs). The Programs provided special education to about 1,100 children from seven counties located throughout Western New York.

The counties that use the Center's preschool special education services pay tuition to the Center using reimbursement rates set by SED. The State, in turn, reimburses the counties for a portion of the tuition paid. SED sets the special education rates based on financial information, including costs, reported by the Center on the annual Consolidated Fiscal Reports (CFRs) that it submits to SED. Costs reported on the CFR must comply fully with the guidelines in SED's Reimbursable Cost Manual (RCM) regarding eligibility and documentation requirements, and must meet the reporting requirements prescribed in the Consolidated Fiscal Reporting and Claiming Manual (CFR Manual). For the fiscal year ended June 30, 2018, the Center reported approximately $9 million in reimbursable costs for the Programs.

# Audit Findings and Recommendations

According to the RCM, costs reported on the CFR are considered for reimbursement if they are reasonable, necessary, directly related to the special education program, and sufficiently documented. For the fiscal year ended June 30, 2018, we identified $272,526 in costs that the Center reported on its CFR that did not comply with SED's requirements for reimbursement, as well as other matters. The ineligible costs include $226,577 in personal service costs and $45,949 in other than personal service (OTPS) costs. Furthermore, our audit identified an error with SED's processing of offsetting revenues reported by the Center that led to the Center receiving $216,451 in excess public funding reimbursements for the three fiscal years ended June 30, 2018.

## Personal Service Costs

For the fiscal year ended June 30, 2018, the Center reported $7.8 million in personal service costs charged to the Programs. We selected judgmental samples of various categories of personal service costs (as described below) and identified $226,577 that was not allowable under SED's requirements.

### Unsupported Costs

According to the RCM, costs must be sufficiently documented to be reimbursable. However, the Center was unable to provide sufficient documentation for $208,482 of the $1,356,981 in personal service costs reviewed to support that these costs were incurred for the Programs as follows:

- $86,731 in personal service salaries and associated fringe benefit expenses for which the Center did not provide required documentation to determine which employees, or in some cases which time period, the expenses were for and, therefore, whether the costs were reimbursable.
- $79,544 in expenses charged to the Programs for non-worked hours (e.g., paid time off, holiday leave) for employees assigned to departments other than those used by the Programs. Center officials stated their practice is to charge an employee's non-worked hours to their base department, including when an employee works in more than one department.
- $8,399 in personal service expenses not supported by time records.
- $17,630 in fringe benefit expenses charged to the Programs for which the Center could not provide sufficient documentation to support the costs were incurred for employees of the Programs.
- $16,178 for salaries and fringe benefits of administrative and non-administrative employees charged to the Programs as a result of discrepancies. These discrepancies include instances where the account listed on the Center's subsidiary payroll ledger differed from the account charged on the general ledger; the department or location listed on the subsidiary payroll ledger was not applicable to the Programs; or the expense should have been allocated across several programs but was solely charged to the Programs.

The RCM states the actual hours of service are the preferred statistical basis upon which to allocate salaries and fringe benefits for shared staff who work on multiple programs. Entities must maintain appropriate documentation such as payroll records or time studies reflecting the hours allocated. The RCM also states that compensation costs must be sufficiently documented and based on approved, documented payrolls and supported by employee time records prepared during, not after, the time period for which the employee was paid. However, during the course of our audit, the Center ended its relationship with the service provider that processed its payroll records during our audit scope period without ensuring it retained access to employee time records required by the RCM to substantiate costs charged on the Center's CFR. As a result, the Center had difficulty obtaining the required support. While the Center was able to obtain payroll time records and approvals for days worked during the period of July 1, 2017 to June 30, 2018, it did not obtain all required documentation. Because the Center operates several affiliated entities that provide services similar to those provided as part of the Programs to other populations of students, without adequate supporting records, we cannot verify the appropriateness of costs reported by the Center on its CFR for the Programs.

## Excess Staffing

SED program approval letters establish direct care student-to-staff ratios for preschool special education classrooms. According to the RCM, direct care personnel costs in excess of the approved ratios are not reimbursable. We compared teacher and teacher aide/assistant staffing levels reported on the Center's CFRs with the relevant SED approval letter and found that the Center exceeded approved staffing, as follows:

- The SED-approved staffing limit for the Center's teacher aides/assistants for the Preschool Special Class – over 2.5 hours per day was 32.91590 full-time equivalents (FTEs). However, the Center reported 33.02800 FTEs on its CFR – an excess of 0.11210 FTEs. The compensation cost for this excess staffing was $2,829 ($2,457 in salaries and $372 in fringe benefits).
- The SED-approved staffing limit for the Center's teachers for the Preschool Integrated Special Class – 2.5 hours per day was 1.04125 FTEs. However, the Center reported 1.1200 FTEs on its CFR – an excess of 0.07875 FTEs. The compensation cost for this excess staffing was $3,791 ($3,343 in salaries and $448 in fringe benefits).

Consequently, we recommend that SED disallow $6,620 ($5,800 in salaries and $820 in fringe benefits) in excess compensation because it did not comply with the RCM's requirements.

## Automobile Allowance

The Center inappropriately reported $5,259 for an automobile allowance paid to its chief executive officer (CEO) as an allowable cost on its CFR. According to the RCM, costs of a personal nature, such as the personal use of a car, known as perks, are not reimbursable. The CEO's employment agreement states the CEO will be provided with an automobile allowance of $750 per month, and the subsidiary payroll ledger also refers to these payments as an automobile allowance. The Center states the automobile allowance is paid as part of the CEO's compensation; however, it did not provide documentation to demonstrate how the automobile allowance payments were used for Center business. We further note that, according to the RCM, the use of privately owned vehicles for program business by employees is reimbursable provided such use is documented and necessary, and the compensated rate does not exceed the mileage rate allowed by the Internal Revenue Service.

### Bonuses

According to the RCM, sign-on and retention bonuses are reimbursable only for direct care titles and must be articulated in a written employer–employee agreement, and sign-on bonuses may be provided only to the position title codes for which the entity has demonstrated difficulty recruiting and/or retaining qualified personnel. Of the $9,250 in bonus payments reviewed, we determined the Center inappropriately reported $5,656 for ineligible bonuses paid to employees on its CFR. This includes $3,116 in bonus payments to two employees who filled positions for which the Center did not demonstrate difficulty in recruitment or retention, a $2,248 bonus payment to one employee that was not articulated in their written employer–employee agreement, and a $292 bonus payment to an employee working in a non-direct care title. Center officials agreed the bonuses paid to non-direct care staff were ineligible for reimbursement, but also stated they retained all necessary documentation to support the sign-on/retention bonuses, including written agreements. However, one of the seven written employer–employee agreements reviewed did not mention the bonus. Moreover, the Center did not provide sufficient documentation showing it faced difficulty recruiting and/or retaining the positions held by the two employees who received a bonus.

### OTPS Allocations

The Center allocates some OTPS administrative costs on the basis of personal service costs. As a result, disallowing personal service costs reduces the amount of allowable OTPS charges to the Programs by $560.

## Other Than Personal Service Costs

For the fiscal year ended June 30, 2018, the Center reported $1.2 million in OTPS costs charged to the Programs. Of this, we judgmentally selected $663,252 in various categories (as described below) and identified $45,949 in OTPS costs that were not allowable under SED's requirements.

### Unsupported Costs

According to the RCM, costs must be sufficiently documented to be reimbursable. We identified $27,436 in OTPS costs for depreciation, consultants, and other undocumented costs ineligible for reimbursement because the Center was unable to provide sufficient supporting documentation.

## Depreciation

We judgmentally selected $56,676 in depreciation costs of the $170,830 total claimed and identified $22,491 in depreciation costs for the acquisition of several fixed assets, including the Center's main administrative building, improvements made to the building, and equipment that did not have the required supporting documentation. According to the RCM, entities operating approved programs are required to retain information relating to the acquisition of fixed assets, equipment, or building improvements, and any related financing arrangements and grants as long as they are used by any education program the provider operates, even if this period exceeds seven years, including building-related documentation such as the purchase agreement. The RCM further stipulates that costs will not be reimbursable on field audit without appropriate written documentation.

The Center was unable to provide required documentation to support the purchase amount of its main administrative building upon which most of the associated depreciation costs reported on its CFR are based. Center officials stated that the documentation supporting the purchase price was not easily retrievable because they were beyond the standard seven-year documentation retention protocols and that the "physical existence of the building is a testament to the underlying purchase expense." Without the required documentation to support the original purchase price of the building, we are unable to verify the accuracy of the depreciation amount. The Center did provide various documentation such as board meeting minutes approving the purchase, a refinancing proposal and confirmation documentation dated approximately two years after the original purchase, audited financial statements, and a depreciation schedule. However, the Center was unable to provide the required documentation to substantiate the original purchase price upon which the depreciation costs are based. Furthermore, the Center could not provide documentation to support the cost of the building improvements included in the depreciated amount.

## Consultants

We judgmentally selected $48,865 in consulting costs from the $106,903 total claimed and identified $3,688 that was not allowable according to the RCM. According to the RCM, the cost of consultant services is reimbursable provided that fees do not exceed the prevailing rate for such services. Adequate documentation to support consultant costs includes the consultant's résumé and a written contract that includes the nature of the services to be provided, the charge per day, and service dates. The Center provided adequate support for most consultant costs in our sample. According to the Center, the consultant costs in question were the result of errors and the Center was unable to provide adequate documentation to support the costs.

### Other Unsupported Expenses

We identified $1,257 in various costs for equipment, supplies, advertising, and travel for which Center officials were unable to provide supporting documentation.

## Allocations

According to the RCM, any expenditures that cannot be charged directly to a specific program must be allocated across all programs that benefit from the expenditure. In addition, entities operating programs must use allocation methods that are fair, reasonable, and documented. In addition to the Programs, the Center operates several other special education programs that serve different populations of children. We found that the Center erroneously included personal service salaries from one of the other programs it offers when allocating costs to the Programs. Furthermore, the Center stated that, in one instance, it used an incorrect method to allocate administrative costs and, in another instance, it erroneously charged the entire amount of an expense to the Programs rather than allocating it across all early childhood programs. As a result of these allocation methodology application errors, we determined $4,356 in ineligible costs were allocated to the Programs.

## Other Ineligible Costs

According to the RCM, costs must be reasonable, necessary, directly related to the special education programs, and sufficiently documented. The RCM states that, when determining the reasonableness of a given cost, consideration is to be given to whether the cost is a type generally recognized as ordinary and necessary for the operation of a special education program approved under Article 89 of New York State Education Law. We determined $14,157 in costs that were ineligible for reimbursement because they were not in compliance with RCM requirements. These costs consisted of:

- $5,577 associated with out-of-state conferences for which the Center could not provide required documentation showing the conferences were critical to the success of the Programs and for services and training that could not be obtained in state.
- $3,143 where the invoices for supplies did not indicate which programs they were for and the employees receiving the supplies were not employees working exclusively in the Programs; or the expenses were not applicable to the Programs, such as a conference fee charged to the Programs even though the subject matter was not relevant to the age range of students served by the Programs.
- $2,971 in ineligible costs that were reversed on the general ledger in a later period but were still reported on the Center’s CFR. In addition, we identified a general ledger transaction for $23 that was charged to the CFR twice, which the Center acknowledged was the result of a clerical error.

- $1,718 for costs that were clinical in nature, including dues to an organization that provides education programs for physicians as well as a subscription for medical appointment phone reminders. These costs appear to align with the Center's clinical operation and not the operation of the Programs.
- $347 in costs related to food for staff development and meetings as well as $166 for anniversary gifts, which are not reimbursable according to the RCM.
- $212 in ineligible costs that the Center self-identified it had failed to back out on its CFR.

# Offsetting Revenues

According to the RCM, any funding from a government 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 the costs will not be reimbursed more than once by public funds. Prior to the 2015-16 school year, revenue for Medicaid fee-for-service and Medicaid managed care was reported on a single line on the CFR. For the 2015-16 school year, special education rate-based providers began reporting each source of Medicaid revenue on separate lines, which was not detected by or reflected in SED's system. Because of this, SED failed to offset $307,735 in Medicaid revenue reported by the Center against program costs, resulting in the Center receiving $216,451 in excess public funding reimbursements. As a result of our audit, SED reported it has corrected the Medicaid reporting issue and anticipates providing additional instruction to its staff going forward.

# Other Related Matters

## Line-of-Credit Interest

According to the RCM, interest costs will be reimbursed only if conditions exist that warrant the principal amount of the loan and the line of credit borrowings are supported by written agreements and documentation showing the necessity for the loan and borrowed amount. The Center uses a line of credit, and Center officials stated it is used to fund operations, including payroll, while awaiting payment from the county. While the Center provided loan statements showing the amount borrowed against the line of credit, the documentation did not show how the Center used the funds for Center operations. The Center has several related entities, and we were unable to determine if the line of credit was used for the Programs and all relevant terms of the RCM were complied with. Therefore, we cannot verify the appropriateness of the $34,588 in interest charged to the Programs.

## Related Parties

According to the CFR Manual, related-party transactions must be reported on the CFR-5 schedule. We found several instances where the Center made payments to related organizations or individuals, including payments to a company whose president is also a member of the Center's Board of Directors. In addition, the Center purchased insurance policies from a company that employs a former (current at the time of purchase) Center board member as a partner. Furthermore, our review of the Center's credit card statements showed transactions involving a restaurant owned by the then-current Chair of the Board of Directors. The Center provided us with an internal control questionnaire, 990 financial statements, and an internal conflict-of-interest memo that showed related organizations and affiliates. However, the Center did not disclose these relationships as related parties on its CFR, as required.

### Competitive Bidding

According to the RCM, competitive bidding practices should be used by all providers when applicable, and the selection of professional services must be done at a minimum of every five years through solicitation of competitive bids. The RCM specifies that bidding documentation must be kept on file by the entities operating the program, and that the entities will need to justify that the consultant hired was the most economical and/or appropriate choice available for a particular service. In response to our request for vendor selection documentation for certain transactions in our sample, the Center was unable to provide documentation in adherence with the RCM guidelines and has maintained that the solicitation of competitive bids was not warranted because it had an established relationship with the vendor. However, Center officials should make use of competitive bidding to ensure that the prices paid for select services and products are the most cost efficient and appropriate for their business, as required by the RCM.

## Recommendations

**To SED:**

1. Review the disallowances identified by our audit and, if warranted, make the necessary adjustments to the costs reported on the Center's CFR and to the Center's tuition reimbursement rates.
2. Make necessary changes to ensure proper calculation of tuition rates and recover overpayments.
3. Remind Center officials of the pertinent SED requirements that relate to the deficiencies we identified.

**To the Center:**

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

# Audit Scope, Objective, and Methodology

The objective of the audit was to determine whether the costs and revenues reported by the Center on its CFR were properly calculated, adequately documented, and allowable under SED guidelines, including the RCM. The audit covered expenses reported on the Center's 2017 and 2018 CFRs for the fiscal year ended June 30, 2018, as well as Medicaid revenues reported for the three fiscal years ended June 30, 2018.

To accomplish our objective and assess internal controls related to our objective, we reviewed the RCM that applied to the year we examined and the CFR Manual and related appendices that applied to the years we examined. We evaluated the Center's internal controls as they related to costs it reported on the CFRs. We reviewed the Center's CFRs for the two calendar years ended December 31, 2018 with a focus on costs for the fiscal year ended June 30, 2018, as well as relevant financial records for the audit period. We also reviewed documentation from SED regarding the offsetting Medicaid revenues reported by the Center for the three fiscal years ended June 30, 2018. We interviewed Center personnel and reviewed policies to obtain an understanding of their financial practices for reporting costs on the CFR. In some cases, we assessed a judgmental sample of costs claimed by the Center for reimbursement based on high risk (e.g., higher dollar amounts, related-party transactions, and costs that appeared not to be relevant to the Programs) to determine whether they were properly calculated, adequately documented, and allowable. Based on our sample design, we cannot project our results to the population as a whole. For other expenses (e.g., bonus payments to indirect staff and senior executive perks), we disallowed costs identified in those categories.

# Statutory Requirements

## Authority

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.

We conducted our performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objective. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objective.

In addition to being the State Auditor, the Comptroller performs certain other constitutionally and statutorily mandated duties as the chief fiscal officer of New York State. These include operating the State's accounting system; preparing the State's financial statements; and approving State contracts, refunds, and other payments. These duties may be considered management functions for purposes of evaluating organizational independence under generally accepted government auditing standards. In our professional judgement, these duties do not affect our ability to conduct this independent performance audit of SED's oversight and administration of the Center's compliance with the RCM.

## Reporting Requirements

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

Within 180 days after final release of this report, as required by Section 170 of the Executive Law, the Commissioner of Education shall report to the Governor, the State Comptroller, and the leaders of the Legislature and fiscal committees, advising what steps were taken to implement the recommendations contained herein, and where recommendations were not implemented, the reasons why.

# Exhibit

## Buffalo Hearing & Speech Center, Inc.
## Schedule of Submitted and Disallowed Program Costs
## for the Fiscal Year Ended June 30, 2018

| Program Costs | Amount per CFR | Amount Disallowed | Amount Remaining | Notes to Exhibit |
|---|---|---|---|---|
| Personal Services | $7,849,685 | $226,577 | $7,623,108 | A, C-F, L, N, O, V |
| Other Than Personal Services | 1,228,678 | 45,949 | 1,182,729 | B, C, G, H, I, K, M, P-W |
| **Total Program Costs** | **$9,078,363** | **$272,526** | **$8,805,837** | |
| Offsetting Revenues | N/A | $216,451* | N/A | J |
| **Net Expenses** | **$9,078,363** | **$488,977** | **N/A** | |

*Offsetting revenue reported by the Center but not offset by SED for the three fiscal years ended June 30, 2018.

# Notes to Exhibit

The following Notes refer to specific sections of the RCM and the CFR Manual 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 Center officials during the course of the audit.

A. RCM Section I.6 – According to the RCM, direct care personnel in excess of or not prescribed by student-to-staff ratios, as defined in a program's approval letter, are not reimbursable unless supported by the student's Individualized Education Program (IEP) requirements and program-generated summary data relating to those IEPs.

B. RCM Section I.10.A – The RCM states that, when determining the reasonableness of a given cost, consideration is to be given to whether the cost is a type generally recognized as ordinary and necessary for the operation of a special education program approved under Article 89 of New York State Education Law.

C. RCM Section II – According to the RCM, costs reported on the CFR are considered for reimbursement if they are reasonable, necessary, directly related to the special education program, and sufficiently documented.

D. RCM Section II.13.A.6 – According to the RCM, costs of a personal nature, such as the personal use of a car, known as perks, are not reimbursable.

E. RCM Section II.13.A.13 – The RCM states that sign-on bonus terms must be articulated in a written employer–employee agreement and a sign-on bonus may be provided only to the position title codes for which the entity has demonstrated difficulty in recruitment and/or retention of qualified personnel.

F. RCM Section II.13.A.14 – According to the RCM, sign-on and retention bonuses are reimbursable only for direct care titles.

G. RCM Section II.14.A.1 – According to the RCM, the cost of consultant services is reimbursable provided that fees do not exceed the prevailing rate for such services. The selection of professional services must be done at a minimum of every five years through solicitation of competitive bids.

H. RCM Section II.22.C – According to the RCM, costs for food provided to any staff and gifts of any kind are non-reimbursable.

I. RCM Section II.28.D.2 – According to the RCM, interest costs will be reimbursed only if conditions exist that warrant the principal amount of the loan.

J. RCM Section II.44.A.2 – According to the RCM, any funding from a government 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 the costs will not be reimbursed more than once by public funds.

K. RCM Section II.59.B – According to the RCM, out-of-state travel should be severely restricted and should be on an exception basis only. Costs associated with such travel 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.

L. RCM Section II.59.D.3 – Use of privately owned vehicles for program business by employees is reimbursable provided such use is documented and necessary. Such use will be compensated at a rate not to exceed the mileage rate allowed by the Internal Revenue Service.

M. RCM Section III.1 – According to the RCM, entities operating approved programs are required to retain information relating to the acquisition of fixed assets, equipment, or building improvements, and any related financing arrangements and grants as long as they are used by any education program the provider operates, even if this period exceeds seven years. The RCM states that costs will not be reimbursable on field audit without appropriate written documentation.

N. RCM Section III.1.A – According to the RCM, compensation costs must be based on approved, documented payrolls and supported by employee time records prepared during, not after, the time period for which the employee was paid. Compensation costs must also be signed by the employee and a supervisor.

O. RCM Section III.1.B – According to the RCM, actual hours of service are the preferred statistical basis upon which to allocate salaries and fringe benefits for shared staff who work on multiple programs. Entities must maintain appropriate documentation reflecting hours used in this calculation. Acceptable documentation may include payroll records or time studies.

P. RCM Section III.1.C.2 – Adequate documentation to support consultant costs includes, but is not limited to, the consultant's résumé and a written contract that includes the nature of the services to be provided, the charge per day, and service dates.

Q. RCM Section III.1.C.3 – The RCM specifies that bidding documentation must be kept on file by the entities operating the program and that the entities will need to justify the consultant hired was the most economical and/or appropriate available for a particular service.

R. RCM Section III.1.D – The RCM requires costs be charged directly to specific programs whenever possible and the particular program(s) must be identified on invoices or associated documents. Competitive bidding practices should be used by all providers when applicable.

S. RCM Section III.1.H.2 – The RCM also specifies that records for working capital loans and lines of credit borrowings must be supported with written agreements and documentation supporting the necessity for the loan and the borrowed amount.

T. RCM Section III.1.K – The RCM states all required documentation to substantiate the purchase of a building be retained as long as the building is used by an approved provider, including a copy of the purchase agreement, deed, any mortgages, and the amortization schedules for such mortgages.

U. RCM Section III.1.M.1 – The RCM mandates expenditures that cannot be charged directly to a specific program be allocated across all programs and/or entities benefited by the expenditure.

V. RCM Section III.1.M.2 – The RCM requires entities to use fair and reasonable allocation methods and such allocation methods, as well as the statistical basis used to calculate allocation percentages, must be documented and retained.

W. CFR Manual Section 18.0, Page 18.1 – According to the CFR Manual, the CFR-5 schedule is used to report all transactions, including compensation, between the reporting entity, its affiliates, principal owners, management, and members of their immediate families and any other party (including an organization) with which the reporting entity may deal when one party has the ability to significantly influence management or operating policies of the other to the extent that one of the transacting parties might be prevented from fully pursuing its own separate interests.

# Agency Comments - State Education Department

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

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

April 26, 2021

Mr. Brian Reilly
Audit Director
Office of the State Comptroller
Division of State Government Accountability
110 State St, 11th Floor
Albany, NY 12236

Dear Mr. Reilly:

The following is the New York State Education Department's (SED) response to the draft audit report, 2020-S-20, Buffalo Hearing & Speech Center, Inc. (Center) - Compliance With the Reimbursable Cost Manual.

Recommendation 1:

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

We agree with this recommendation. SED will review the recommended disallowances as noted in the report and make adjustments to the reported costs to recover any overpayments, as appropriate, by recalculating tuition rates. NYSED will further review the staffing recommendations to determine if the adjustments are appropriate.

Recommendation 2:

"Make necessary changes to ensure proper calculation of tuition rates and recover overpayments."

We agree with this recommendation. SED will review the recommended disallowances as noted in the report and make adjustments to the reported costs to recover any overpayments, as appropriate, by recalculating tuition rates.

Recommendation 3:

"Remind Center 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 Center's officials avail themselves of our assistance to help them better understand the rules for cost reporting and criteria for cost reimbursement as presented in the CFR, Regulation and the Reimbursable Cost Manual (RCM). Furthermore, SED will alert the Center of online CFR training that is available on SED's webpage. SED recommends that all individuals signing the CFR certification statements, namely the Executive Director and Certified Public Accountant, complete this training. This training is a requirement for preschool special education providers upon approval and reapproval.

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

Sincerely,

Sharon Cates-Williams

Sharon Cates-Williams

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April 26, 2021

Brian Reilly
Office of the State Comptroller
Division of State Government Accountability
110 State Street, 11th Floor
Albany, NY 12236

Re: State Education Department
Compliance with the Reimbursable Cost Manual
Buffalo Hearing and Speech Center (the "Center")
Audit Report 2020-S-020
Draft Report

Dear Mr. Reilly:

We have reviewed the above-referenced Draft Report concerning whether the costs and revenue reported by the Buffalo Hearing and Speech Center (the "Center") on its Consolidated Fiscal Report (CFR) for the years 2017 and 2018 were properly calculated, adequately documented, and allowable under the State Education Department's ("SED's") guidelines, including the Reimbursable Cost Manual ("RCM"), for the fiscal year ending June 30, 2018, as well as revenue reported for the three fiscal years ending June 30, 2018. While we do not challenge many of the proposed findings as set out below, we do challenge select findings, whole or in part.

**Personal Service Costs**

**Unsupported Costs**

As the auditors are fully aware, BHSC experienced certain challenges to accessing its payroll records maintained by an outside vendor for the audit years, having even requesting the Office's assistance in securing access to our records through any means possible. After a significant delay, BHSC was able to share with the audit team access to numerous records in support of personal service expenses. We trust that the auditors' review of these delayed records was extensive and thorough, notwithstanding time constraints.

**State Comptroller's Comment** – OSC granted Center officials multiple extensions of time to provide additional documentation in response to our preliminary findings covering personal service expenses. OSC auditors completed an extensive review and gave appropriate consideration to all additional information provided by the Center. We adjusted the draft audit report, where relevant, to reflect the supplemental information that the Center provided during the nearly 6-month period after the preliminary findings were issued.

BHSC does not challenge the proposed disallowance of **$17,630** in fringe benefit expenses for which we remain unable to retrieve supporting documentation.

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As relates to **$86,731** in personal service salaries and associated fringe benefit expenses for which the auditors assert inadequate documentation was provided, BHSC reasserts its challenge of **$54,581** in proposed disallowances associated with certain individuals. BHSC has made certain adjustments to entries to correct location and program code designations of select individuals, as reflected in the attached documentation **(See: Attachment Exhibit A; Summary Tab).** We have also resubmitted the time records **(See: Attachment PS-26, PS-27, PS-28, PS-29 Timesheet)** in support of **$54,581**. As we shared with the auditors, BHSC had made adjustments to the GL to reflect corrections made by supervisory staff upon review of the full semester's timesheets. These corrections were not made on the timesheets themselves, however. Thus, the time records as reviewed, the auditors argue, do not appear to support the costs as allocated by the Center. We assert that the time records, as corrected on the general ledger, support the full $54,581.

**State Comptroller's Comment** – The Center had numerous opportunities to provide documentation to support the expenses in question. We originally requested supporting documentation in June 2020 and followed up with Center officials in July, August, September, October, November, and December 2020. However, after these multiple requests, adequate supporting documentation was not provided. We question the timeliness of the additional documentation provided after the draft report was released. As a result of the delay, we cannot verify whether the documentation provided in response to the draft report was prepared during, and not after, the time period for which the employees were paid, as required by the RCM. Further, the documentation does not show how adjustments were calculated.

BHSC further challenges the auditors' proposed disallowance of **$16,178** for certain administrative and non-administrative employees charged to the program as a result of discrepancies. As BHSC has shared with the auditors, the expenses were incurred exclusively for the benefit of the 9100 program – the single program in operation at that site location. BHSC had shared with the auditors' proof of the adjustment through a series of entries in the general ledger with explanations of the allocations by classroom. We resubmit that documentation here **(See: Attachment Exhibit A; Summary Tab).** We also resubmit supporting records which the auditors may not have reviewed **(See: Attachment See: PS-12 Timesheet).**

**State Comptroller's Comment** – Despite numerous conversations and correspondence, the Center appears to have confused the expenses in question. The $16,178 disallowance was not related to the attachments the Center refers to in its response. Furthermore, the Center's own general ledger data shows multiple other programs at the location in question, not the single program as the Center indicates in its response.

BHSC also challenges the proposed disallowance of **$79,544** in expenses charged to the audited programs for non-worked hours. As shared with auditors, the "home department" data reviewed by the team represented a default setting to the current home department designations. The payroll provider presented the requested records under the current home department only rather than under the home designation during the audit years. As a result, the auditors identified a good number of discrepancies which we assert are easily explained upon review of actual historical data – the home department designations as made during the audit years. Only upon review of the historical data can the auditors appropriately recognize the documentation in support of **$70,300** of the **$79,544** in proposed disallowances. **(See: Attachment Exhibit A; Summary Tab)**

Again, many of the discrepancies identified by the auditors are the result of the payroll provider's formatting error. More specifically, the "home department" designation referenced above, once recorded by the payroll provider, remained unchanged in that payroll report, although correctly revised in BHSC's own records. Moreover, while BHSC concedes it did not anticipate the failure of the payroll provider to gain access to our own records, BHSC did retain comprehensive time sheets, session notes, and other documentation in support of such costs. We believe strongly that any "gaps" in required documentation occasioned by the severed relationship with the payroll provider were addressed by volumes of secondary support.

More specifically, we resubmit time records in support of **$46,338** of the proposed **$52,499** – other PS non – sample, together with documentation reflecting the historical home department – the correct home department designations – as differentiated from the misleading home department assigned by the vendor payroll provider **(See: Attachment See Exhibit A; Summary Tab)**.

We likewise submit time records in support of **$12,988** of the proposed **$16,211** disallowance again reflecting historical home department assignment as contrasted with the misleading default setting home department representation provided by the payroll provider **(See: Attachment Exhibit A; Summary Tab).**

**State Comptroller's Comment** – The audit team met and corresponded with the Center throughout the audit to help ensure that Center personnel fully understood our application of audit criteria from the RCM. We also granted Center officials multiple extensions of time to provide additional documentation in response to our preliminary findings, as noted in our earlier comments. Furthermore, the RCM states that compensation costs must be based on approved, documented payrolls and payroll must be supported by employee time records. It is the Center's responsibility to ensure the accuracy of these time records, not the payroll provider that processes the data input by the Center. Center officials did not retain comprehensive time sheets, as noted in their own comments regarding the inability to gain access to their own records. The Center retained and provided us with only a general and subsidiary ledger; however, these are not sufficient to support payroll expenses. Additionally, neither session notes nor the historical data referenced by the Center in its response were provided to the auditors during the course of the audit.

**Excess Staffing**

BHSC does not challenge the proposed disallowance of **$3,791** associated with teaching staff for the SCIS program.

As related to the proposed disallowance of **$2,829** associated with teacher aides/assistants for the SC program, we request that the auditors reexamine the disallowances to assure there is no unintended duplication as a result of any "home department" disallowance.

**State Comptroller's Comment** – The audit team accounted for and removed these individuals from our analysis, as explained to Center officials in December 2020.

**Automobile Allowance**

While BHSC concedes that the applicable provisions of the COO's engagement letter/agreement around vehicle expenses could have been presented more precisely, the expense was at all times included within reported compensation, appropriately taxed, and always within median salary parameters. BHSC also believes that the internal representation of the expenses as "auto allowance" may be contributing to the auditors' determination. The mischaracterization of the expense as an auto allowance on the payroll ledger was simply perpetuated.

In fact, the auditors' characterization of the expense as a "perk" is inconsistent with the provisions of the RCM which prescribe "expenses of a personal nature, such as a residence or personal use of a car." Simply stated, additional compensation for expenses associated with a vehicle is not contemplated within the intended context of the RCM prescription, especially where, as here, the expense reimbursement is clearly included on payroll documents and appropriately taxed. The very wording of the employment agreement provision reflects the underlying program/business nature of the expense – "as the senior executive in this organization" – in clear contradiction of any personal nature as prescribed by the RCM. Accordingly, we would argue that proposed disallowance be restored.

**State Comptroller's Comment** – According to the RCM, use of privately owned vehicles for program business by employees is reimbursable provided such use is documented, necessary, and compensated at a rate not to exceed the mileage rate allowed by the IRS. The Center never provided any documentation, such as vehicle logs, to show how the vehicle was used for business purposes. Furthermore, the Center's own documentation listed the expense as an automobile allowance.

**Sign-on and Retention Bonuses**

BHSC challenges certain of the auditors' findings as relates to sign-on and retention bonuses, conceding that awards to non-direct care employees, while necessary, should have been reported as non-reimbursable expenses. BHSC retained all necessary documentation in support of the sign-on/retention bonuses, including written agreements. As to the RCM association of demonstrated difficulty in recruitment with the propriety of the award, BHSC's demonstrated staff turnover, documented staff shortages in the region for specific credentialed professionals, and BHSC's receipt of ETTP funding (excessive teacher turnover prevention grants) are all testament to the need for such bonuses. BHSC's efforts to provide "turnover" data per se, as requested by the auditors, had been compromised as a result of our continued denial of access to that information maintained in our payroll system for the audit years by the prior payroll vendor. However, BHSC did reconstruct aspects of staffing patterns provided to the audit team which reflect solicitations of "new hires" and new hire and recruitment patterns, in support of the bonus.

**State Comptroller's Comment** – According to the RCM, sign-on bonus terms must be articulated in a written employer–employee agreement and may be provided only for the position title codes for which the entity has demonstrated difficulty in recruitment and/or retention of qualified personnel. As noted in the report, one of the seven written employer–employee agreements reviewed did not mention the bonus. Further, while Center officials did provide documentation showing they recruited for two other positions in which the employees received a bonus, they did not provide sufficient documentation showing they faced difficulty recruiting and/or retaining those positions, as required by the RCM.

**OTPS Allocation**

We appreciate the audit teams' reassessment of the proposed disallowance relating to OTPS allocations, based upon favorable review of the salary expense supporting documentation.

**Other-Than-Personal Service Costs**

**Unsupported Costs**
*Depreciation*

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BHSC appreciates the auditors' acknowledgement of the comprehensive set of documents provided in support of the reported depreciation costs including Board minutes in which the purchase price was clearly stated, consolidated balance sheets from audited financials reflecting the property, documentation around the mortgage offer with interest rate, and requisite depreciation schedule. We believe taken together, this documentation more that adequately supports the reported depreciation costs. Each of these documents reflects the stated purchase price which was clearly fixed, the value of which is reflected in all fixed asset records. We do not believe either the intent nor the wording of the RCM requirement is advanced by the denial of the several, for want of a single document.

**State Comptroller's Comment** – As noted in the report, the RCM states that entities operating approved programs are required to retain information relating to the acquisition of fixed assets, equipment, or building improvements, and any related financing arrangements, including building-related documentation such as the purchase agreement, as long as they are used by any education program the provider operates, even if this period exceeds seven years. We are disappointed Center officials characterize the issue as "for want of a single document." The Center was unable to provide documentation supporting the actual acquisition costs, reflecting the original purchase and development costs of the building upon which the depreciation costs are based. Furthermore, the Center's own response to our preliminary findings stated that documentation to support the construction of the Center was not easily retrievable after seven years.

*Consultants*

BHSC does not challenge the proposed disallowance of **$3,688** associated with consulting costs for which we were unable to provide adequate supporting documentation and appreciate the acknowledgement that BHSC did provide adequate support for most consultant costs.

*Other Unsupported Expenses*

BHSC does not challenge the **$1,257** proposed disallowance for equipment, supplies, advertising and travel for which adequate documentation was unavailable.

**Allocations**

BHSC does not challenge the remaining **$4,356** in challenged allocation costs which are attributed to clerical errors.

**Other Ineligible Costs**

BHSC does not challenge:

- **$5,577** in proposed disallowance associated with staff attendance at an out-of-state conference, while reasserting the fact that the conference host sets the annual conference throughout the country for the very fact that the subject matter is of national appeal to the community of service providers. To be fair, it is quite impossible to prove that another "like" conference was not available in New York, akin to proving a negative;

- **$3,143** in proposed disallowance associated with supplies or attendance of a staff member at "non-relevant" conference, while again asserting the relevance of the conference to the community of service providers;

- **$2,971** in costs which were revised on the general ledger in a later period but inadvertently reported on the CFR;

- **$1,718** in costs more likely associated with BHSC's clinical operations;
- **$347** in costs related to food for staff development and $166 for employment anniversary acknowledgements, although well deserved, not eligible for reimbursement; and
- **$212** in reported costs BHSC inadvertently failed to have been backed out on the CFR.

**Offsetting Revenue**

BHSC appreciates the auditors' acknowledgement that while the Center properly reported Medicaid fees for service revenue on its CFR, SED failed to offset said revenue against program cost due to an error in the SED process.

**Other Related Matters**

**Line of Credit Interest**

BHSC reasserts its position that it is not one single expense nor any single principal advance that accounts for the need to access the line of credit. The reliance on the line of credit is a function of an institutional operational deficit which is only contained and managed by the line. BHSC is often compelled to rely on the continuing fiscal support of its line of credit to supplement the reimbursement for services not adequately supported by tuition rates, to fund operations while awaiting payments from the counties and to generally address the constant misalignment between costs and reimbursement. BHSC shared with the audit team substantial documentation including loan statements around borrowing and repayments, applicable interest rates and such other documents in support of the amounts accessed on the line of credit including a sample cash flow received as disbursement from the line of credit. We believe strongly that these documents confirm the appropriateness of the $34,588 in interest charged.

**State Comptroller's Comment** – While the Center provided us with documentation in regard to the line of credit, the documentation did not show a specific accounting of the funds drawn from its line of credit to support that the funds were used for Program operations.

**Related Parties**

BHSC reasserts its position of full disclosure of any and all related party transactions, as supported by internal control questionnaires, 990 financial statements, and conflict of interest disclosure forms and policies.

**State Comptroller's Comment** – As noted in the report, while several related-party transactions were disclosed on the internal control questionnaires, 990 financial statements, and conflict of interest disclosure forms, they were not disclosed on the CFR, as required.

**Competitive Bidding**

BHSC acknowledges the auditors' recommendation to make use of competitive bidding to ensure that prices paid for select services and products are the most cost-efficient and appropriate for our operations, as a complement to our own solicitation protocols and long-standing vendor relations.

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Brian Reilly
Office of the State Comptroller
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We appreciate the opportunity to provide comment on the proposed findings.

Very truly yours,

GREENBERG TRAURIG, LLP

PAM/maf
Enclosures
*ACTIVE 56605056v1*

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