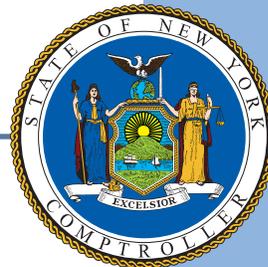


2015 Annual Report on Preschool Special Education Audit Initiative

OFFICE OF THE NEW YORK STATE COMPTROLLER

Thomas P. DiNapoli, State Comptroller



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A MESSAGE FROM COMPTROLLER THOMAS P. DiNAPOLI

Special education programs fulfill a great need across New York State, but too often taxpayers are paying for more than they should. Our audits have found that while many private special education providers use public funds conscientiously and in accordance with State rules, others evade the rules and abuse taxpayer funds.



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. Our audits have identified problems with the accuracy and appropriateness of self-reported program costs, as well as the effectiveness of program monitoring and oversight. As a result, children needing special education services have been shortchanged by certain private providers who used public funds inappropriately.

The State Legislature responded to this pattern of abuse by passing legislation requiring my office to audit the expenses submitted to the State Education Department (SED) by every provider of preschool special education services at least once by March 31, 2018, and to report annually on the findings of our audits to the Governor and the Legislature. This report is the second such annual report.

We coordinate our audit efforts with the State Education Department, the New York City Department of Education, the New York State Association of Counties, and the counties themselves, to improve the oversight and management of this important sector. 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.

Although recent audits have continued to find problems similar to those discovered by the audits completed in previous years, the audits completed in 2015 show indications that there is some improvement in cost reporting by preschool special education providers to SED. As a result of the work of this office and the combined commitment of all responsible parties, these audits continue to have a far-reaching impact on the State's efforts to strengthen the oversight of preschool special education providers in New York.

As New York continues to monitor preschool special education, it is important that all stakeholders commit long-term to making this important sector of the State's education system work more efficiently and effectively. For our part, my office will continue to promote best practices and to emphasize the importance of critical internal controls and responsible external oversight.

NEW YORK STATE PRESCHOOL SPECIAL EDUCATION AUDIT INITIATIVE

EXECUTIVE SUMMARY

New York State has a long history of providing special education services to students with disabilities. 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 81,000 preschool students with disabilities receive services in New York at an annual cost of almost \$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 provider compliance with SED cost-reporting guidelines and the accuracy and appropriateness of self-reported program costs. These audits identified a widespread pattern of unsupported expenditures, expenses claimed from other programs, personal expenses included with program expenses, no-show jobs, and less-than-arm's-length transactions. OSC concluded that stopping fraudulent, wasteful, and abusive practices by preschool special education 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 providers. As a result, Chapter 545 of the Laws of 2013 was signed into law on December 18, 2013 and became effective immediately. 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 by March 31, 2018, "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 twelve months.

As of December 2015, OSC has completed 63 audits of expenses submitted to SED by preschool and/or school age special education providers over the last decade, including 23 completed in 2015. These audits have cumulatively identified almost \$52 million in disallowances, or 6 percent of the total claimed expenses of \$845 million. OSC also conducted an audit of SED's fiscal and program oversight of special education providers and issued an audit report thereon in December 2012.

The audits completed in 2015 have continued to find problems akin to those found in the audits completed in previous years. However, these recent audits show indications that there is some improvement in cost reporting by the preschool special education providers to SED. As a result of the leadership of this Office and the combined commitment of responsible parties, these audits continue to have a far-reaching impact on the State's efforts to strengthen the oversight of preschool special education providers in New York.

OVERVIEW

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 IDEA, parents of children with disabilities in New York State petitioned 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 of this legislation, 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 were required to continue to pay for special education services for preschoolers while receiving partial reimbursement from the State.

Currently, the New York State Education Department (SED) reports that about 81,000 preschool students with disabilities receive services throughout the State annually. Preschool students with disabilities may receive related services only, services of a Special Education Itinerant Teacher (SEIT) or be placed in a special class program for either half or full day, including integrated programs for students without disabilities when appropriate. New York's system allows for the provision of related services and SEIT 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 almost \$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 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 Manual) and the Reimbursable Cost Manual (RCM). 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 to SED by preschool special education providers which focused on compliance with SED cost-reporting guidelines and the accuracy and appropriateness of self-reported program costs. These audits identified a pattern of unsupported expenditures,

expenses claimed from other programs, personal expenses included with program expenses, no-show jobs, and less-than-arm's-length transactions. OSC concluded that stopping fraudulent, wasteful and abusive practices by these providers required a more comprehensive approach.

In June 2012, Comptroller DiNapoli announced a special education audit initiative which involved a broader, sector-wide perspective as well as multiple simultaneous individual audits, 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. Comptroller DiNapoli also proposed legislation to improve the oversight of public funding for preschool special education providers.

Chapter 545 Legislation

Chapter 545 of the Laws of 2013 was signed into law on December 18, 2013 and became effective immediately. 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 by March 31, 2018, "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 twelve months and regarding any other pertinent information the comptroller deems appropriate." This report fulfills the statutory reporting requirement under Chapter 545 for 2015.

Chapter 545 also directed SED to conduct a comprehensive study of alternative systems of reimbursement methodologies and monitoring protocols for 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 clause (C) to subparagraph (i) of paragraph a of subdivision 10 as follows: "Notwithstanding any other provision of law, rule or regulation to the contrary, on or before the 2016-17 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 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 Chapter 545, OSC developed a risk assessment process to prioritize the preschool special education audits to be undertaken according to 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 management with the identification of high-risk special education providers 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 its own 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 steps in the OSC audit process, from the issuance of an engagement letter through the release of a final report. The training also addresses the State's expectations of providers. During 2015, OSC provided 6 training sessions to 227 staff representing 84 special education providers. In addition, about 330 Executive Directors, administrative staff and certified public accountants (CPAs) affiliated with providers have participated in CFR training conducted by SED during 2015.

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, called "OSC Special Education Initiative," 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.

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. 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. Chapter 57 of the Laws of 2013 included provisions to authorize a municipality to retain 100 percent of recoveries identified by its audits. The New York City DOE and the counties of Monroe and Suffolk conduct their own fiscal audits of local preschool special education programs delivering services within their jurisdictions.

AUDIT FINDINGS

In 2015, OSC completed 23 audits of expenses submitted to SED by preschool special education providers. These audits have cumulatively identified over \$10 million in disallowances, or about

3.4 percent of the total claimed expenses of almost \$301 million for the audit period. Fifteen providers had between 2.1 percent and 7.2 percent of claimed expenses disallowed. Eight of the 23 preschool special education providers had 1.2 percent or less of claimed expenses disallowed. There are currently 19 additional audits in progress.

These findings of disallowed expenses range from 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 abuse of funds intended for the education of children with disabilities, as well as outright fraud. However, the audits completed in 2015 show there is some improvement in cost reporting by the preschool special education providers to SED, as noted in the sections below.

The 2015 audit findings can be summarized as follows:

Personal Service-Related Findings – OSC audits completed in 2015 identified \$2.2 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 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. Over half of the audits (14 out of 23) found issues with the maintenance of payroll and time distribution documentation as required by the RCM. This is slightly higher than the number of problems reported in 2014.
- **Unsupported bonuses** – SED requires that salary bonuses be based on merit and supported by performance evaluations to be eligible for reimbursement. More than a half of the audits (14 out of 23) found evidence of bonuses that were not in compliance with the RCM. This is about a 20 percent increase from the number of incidents reported in 2014.

Other Than Personal Service (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 (preschool) special education program and properly documented. In addition, expenses of a personal nature are not reimbursable. OSC audits completed in 2015 identified almost \$2.8 million in unsupported or ineligible OTPS-related expenses:

- **Vehicles** – 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 travelers for individual vehicles. Over half of the audits (12 out of 23) identified disallowances of vehicle-related expenses which were inadequately documented or otherwise ineligible for reimbursement, a slight increase from the number of problems reported in 2014.

- **Travel** – Travel costs must be program-related and appropriately documented to be eligible for reimbursement. Similar to the number of problems reported in 2014, more than a third of the audits (10 out of 23) disallowed ineligible travel costs of staff, family members and/or non-employees.
- **Expenses of a personal nature** – Personal expenses are not eligible for reimbursement. In 5 out of 23 audits, personal expenses were disallowed for such purchases as staff development, phone costs, and fines – a significant improvement from the number of problems reported in 2014.
- **Inadequate Documentation** – SED guidelines require that expenditures be reasonable, necessary, directly related to the program and adequately documented in order to be considered for reimbursement. In nearly all of the audited programs (20 out of 23), there were findings of ineligible expenses which were either not program-related or were not supported by adequate documentation. However, the 2015 audits found a significant decrease in the dollar amount (materiality) of the findings. The findings decreased in dollar value from a total of \$16 million to about \$477,000. This includes \$165,595 for costs related to staff food and entertainment compared to the more than \$760,000 for such costs disallowed in prior periods.
- **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. Findings in this cost category were not included in the 2014 report; in 2015, 8 of the 23 audits noted disallowances for consultant services.

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 which 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. Over half of the audits completed in 2015 (16 out of 23) identified problems related to the allocation of costs among programs and/or the inappropriate claiming of expenses from other programs – a substantial increase from the number reported in 2014. The disallowances totaled almost \$5.2 million or over half of all disallowances reported in 2015.

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). Two of the 23 audits identified issues related to allocation

of costs between direct and non-direct care – a significant decrease from the levels reported in 2014.

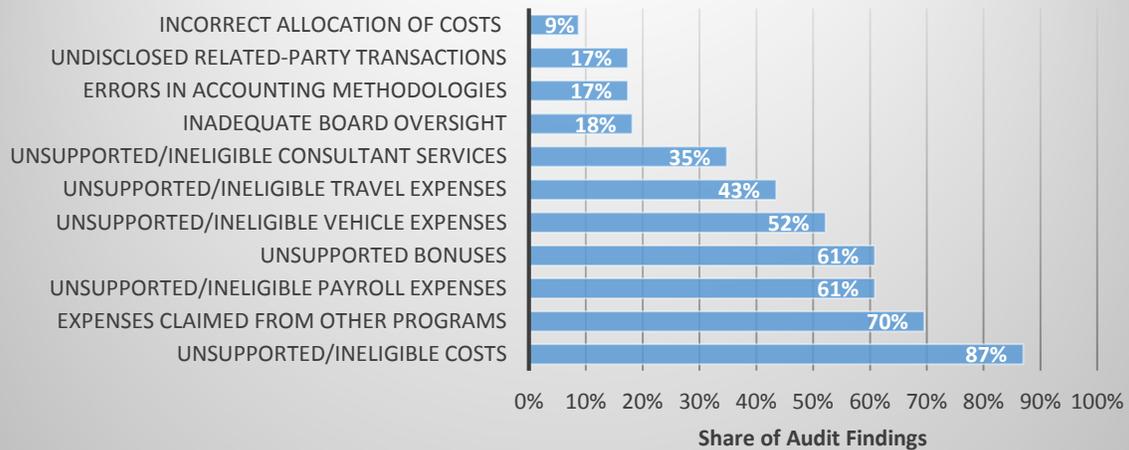
Undisclosed Less-Than-Arm’s-Length (LTAL) Transactions – SED requires special education providers to disclose all less-than-arm’s-length (LTAL) transactions in their CFRs and in the notes to their financial statements. In brief, a LTAL relationship exists when there are related parties and one party 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. Last year, OSC reported that more than a third of the audits (13 out of 37) identified LTAL transactions which were not disclosed as required. In 2015, 4 out of 23 audits identified LTAL transactions which were not disclosed as required.

Errors in Accounting 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. Four out of 23 audits found the inappropriate expensing of such costs – an improvement from the number of problems noted in 2014.

Oversight by Boards of Directors and Systems of Internal Controls – When providers are overseen by boards of directors, board members are subject to certain obligations, 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 11 of the 23 audits conducted in 2015, the providers were overseen by boards of directors. OSC audits reported that only one of those boards of directors did not provide adequate oversight – an improvement over last year. The RCM also requires all entities operating SED programs to establish adequate systems of internal controls and to conduct annual risk assessments. OSC audits identified one provider which had not established formal policies or procedures for certain critical business functions, nor had the provider ever performed a formal risk assessment.

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 have found numerous errors in cost reporting in CFRs that can be attributed to the lack of due diligence by CPAs hired by special education providers. Examples include: instances of personal expenses included with program expenses; LTAL transactions; errors in allocation methodologies; and errors in accounting methodologies used for depreciation, amortization, and accruals. Although the audits completed in 2015 found improvements in these areas, OSC will continue to closely monitor the role of CPAs in the CFR submission process.

Patterns of Disallowances Among Special Education Providers in New York State



Special Education Program Audits Completed in 2015

In 2015, OSC completed 23 audits of expenses submitted to SED by special education providers. The recent audits have continued to find problems similar to the audits completed in previous years. However, the audits completed in 2015 show indications that there is some improvement in cost reporting by the preschool special education providers to SED. The 23 completed audits are summarized in the following narratives.

Clinical Associates of the Finger Lakes (Clinical Associates) (2014-S-61) is a privately owned institution located in Victor, New York, that offers a wide range of services for children with disabilities from birth through age five. Programs include the SEIT Program, Preschool Evaluation Program, Preschool Related Service Program, One to One Aide Program, and Early Intervention Program. For the fiscal year ended June 30, 2013, Clinical Associates reported \$1.2 million in reimbursable costs for its SEIT Program. The OSC audit recommended disallowances of \$72,401 in costs charged to the SEIT program that did not comply with SED's requirements for reimbursement, including:

- \$45,628 for building and administrative costs that were over-allocated to the SEIT program; and
- \$9,123 in OTPS expenses that were either non-reimbursable or lacked supporting documentation. (Note: prior to the OSC audit SED adjusted a portion of these expenses.)

OSC's audit report also found that Clinical Associates had not established formal policies or procedures for some critical business practices and had never performed a formal risk assessment.

Hear 2 Learn PLLC (Hear 2 Learn) (2014-S-74) is a privately owned institution located in Syracuse, New York, that provides a wide range of services and programs to children with disabilities from birth through age five that include the SEIT program. For the fiscal year ended June 30, 2013, Hear 2 Learn reported \$2.7 million in reimbursable costs, of which \$340,876 was for its SEIT program. The OSC audit recommended disallowances of \$20,851 in costs charged to the SEIT program that did not comply with SED's requirements for reimbursement, including:

- \$9,894 in personal services costs that included undocumented salary and related fringe benefit costs allocated to the SEIT program; and
- \$7,264 for facility-related costs charged at a location where Hear 2 Learn does not provide SEIT services.

Inspire (Orange County Cerebral Palsy Association) (2014-S-80) is a non-profit organization that provides a wide array of outpatient, education, and support services for individuals of all ages and abilities. Currently, Inspire operates preschool special education programs for children with disabilities between the ages of three and five years at sites in Goshen, Newburgh, and Monroe, New York. Inspire reported over \$6.4 million in reimbursable costs for its special education programs for the fiscal year ended June 30, 2013. The OSC audit recommended disallowances of \$226,382 in costs that did not comply with SED's requirements for reimbursement, including:

- \$149,768 in bonuses and fringe benefits costs that were unsupported or paid to staff who did not work in the preschool special education program;
- \$31,359 in vehicle and travel costs that were not properly documented;
- \$30,855 in costs that were not related to the special education programs; and
- \$14,400 for staff food, entertainment and gifts.

The OSC audit also noted Inspire did not comply with provisions of the RCM, the CFR Manual, and other SED requirements pertaining to the disclosure of less-than-arm's-length business transactions and the reporting of direct and indirect costs on the CFR.

Kew Gardens SEP, Inc. (Kew Gardens) (2014-S-63) is a for-profit organization located in Queens, New York, that provides preschool special education services to children ages three through five years. For the three fiscal years ended June 30, 2013, Kew Gardens reported approximately \$9.8 million in reimbursable costs for its preschool special education programs. The OSC audit scope period focused on the 2012-13 fiscal year, and included certain items claimed on the CFRs for the 2010-11 and 2011-12 fiscal years. The OSC audit recommended disallowances of \$295,997 in reported costs that did not comply with SED's requirements for reimbursement, including:

- \$119,906 in accrued pension plan expenses for a plan that was not yet established and later distributed as wages or used to reduce a prior period's liability.
- \$93,771 for accrued compensation paid to 19 employees in subsequent years that were not added to the employees' base compensation. As such, the payments in question met

the RCM's definition of bonuses. However, there were no formal performance evaluations, as otherwise required, to support the payments.

- \$50,851 for excess retirement plan contributions for employees.
- \$19,120 for salary expenses paid to employees whose timesheets showed they worked the same 12:00 p.m. – 2:00 p.m. time period at another preschool provider.

Kids-Centric, Inc. (Kids-Centric) (2014-S-73) is a for-profit organization based in Brooklyn, New York, that provides preschool special education programs to children ages three through five years old. For the three fiscal years ended June 30, 2013, Kids-Centric reported approximately \$14.2 million in reimbursable costs for its preschool special education programs. The OSC audit scope period focused primarily on fiscal year 2012-13. However, OSC expanded its review to include certain items claimed on the CFRs for fiscal years 2010-11 and 2011-12. The OSC audit recommended disallowances of \$301,601 in reported costs that did not comply with SED's requirements for reimbursement, including:

- \$67,783 in unsupported and ineligible travel expenses;
- \$58,565 in unsupported salary expenses;
- \$36,812 in salaries and fringe benefits costs, and equipment and supplies that were already funded from federal IDEA grants;
- \$39,895 in employee bonuses that were not supported by performance evaluations or exceeded salary limits; and
- \$39,410 in food expenses related to staff meetings, staff parties (including alcohol) and personal restaurant charges.

Mid Island Therapy Associates, LLC (Mid Island), aka, All About Kids (Report 2014-S-40) is a for-profit organization located in Plainview, New York, that provides a number of services to disabled children from birth through five years of age, including preschool special education programs. For the three fiscal years ended June 30, 2013, Mid Island claimed approximately \$10.6 million in costs for the preschool special education programs. The OSC audit scope period focused primarily on fiscal year 2012-13. However, OSC expanded its review to include certain items claimed on the CFRs for fiscal years 2010-11 and 2011-12. The OSC audit recommended disallowances of \$655,055 in reported costs that did not comply with SED's requirements, including:

- \$466,575 in salary and fringe benefits from other programs that were over-allocated to the preschool special education program;
- \$147,121 in non-allowable retroactive salary increases;
- \$18,259 in rental expense from other programs allocated to the preschool programs; and
- \$15,605 in expenses that were ineligible or undocumented, including vehicle costs, travel costs, and non-special education program-related costs.

Milestone School for Childhood Development (Milestone) (2014-S-37) is a for-profit organization that provides full-day preschool center-based and integrated special education programs to children ages three through five years. For the three fiscal years ended June 30, 2013, Milestone reported approximately \$11.1 million in reimbursable costs for its preschool special education programs. The OSC audit scope period focused primarily on fiscal year 2012-13. However, OSC expanded its review to include certain items claimed on the CFRs for fiscal years 2010-11 and 2011-12. The OSC audit recommended disallowances of \$801,859 in reported costs that did not comply with SED's requirements for reimbursement, including:

- \$196,610 in excessive lease costs charged to the programs;
- \$188,447 in OTPS costs, such as telephone expenses, depreciation, and American Express charges, that lacked supporting documentation;
- \$149,815 in unsupported or inappropriate fringe benefit costs;
- \$105,632 in over-allocated compensation costs for three employees who also worked at Milestone affiliates; and
- \$63,310 in charges that were not incurred, including voided checks and duplicate payments to vendors.

Rivendell School (Rivendell) (2015-S-25) is a not-for-profit organization based in Brooklyn, New York, that offers a range of educational programs including preschool special education services to disabled children from three to five years of age. For the three fiscal years ended June 30, 2014, Rivendell reported approximately \$7.5 million in reimbursable costs for its preschool programs. The OSC audit recommended disallowances of \$536,449 that did not comply with SED's requirements, including:

- \$389,012 in costs over-allocated to the preschool special education program;
- \$70,644 in extra pay expenses that were undocumented or unrelated to the preschool special education program; and
- \$12,699 in unnecessary and ineligible travel costs.

Starting Point Services for Children (Starting Point) (2014-S-64) is a not-for-profit organization based in Brooklyn, New York, that provides a range of programs including preschool special education services to disabled children ages three to five years. For the fiscal year ended June 30, 2013, Starting Point reported approximately \$16.4 million in reimbursable costs for its preschool special education programs. The OSC audit scope period focused primarily on fiscal year 2012-13. However, OSC expanded its review to include certain items claimed on the CFRs for fiscal years 2010-11 and 2011-12. The OSC audit recommended disallowances of \$2,585,454 in reported costs that did not comply with SED's requirements for reimbursement, including:

- \$1,981,802 in non-reimbursable shared staff compensation costs because Starting Point overstated the number of hours allowable to the programs audited by 34,810 hours;

- \$310,136 in consultant costs that did not document the specific services provided and the hourly fee charged;
- \$173,539 in unsupported bonuses to staff;
- \$70,078 for salaries and fringe benefits for employees who worked in another program; and
- \$49,899 in other ineligible costs, including \$22,245 for meals provided to staff.

United Community Services, Inc. (United) (2015-S-44) is a for-profit organization based in Brooklyn, New York, that provides a range of education programs including preschool special education programs to disabled children ages three through five years. United has a collaboration agreement with Bushwick United Headstart (Bushwick) and provides services to disabled students at four Bushwick locations. For the three fiscal years ended June 30, 2014, United reported approximately \$7.3 million in reimbursable costs for its programs. The OSC audit recommended disallowances of \$207,295 in reported costs that did not comply with SED's requirements for reimbursement, including:

- \$81,068 in compensation paid to the Assistant Executive Director (AED). This individual's timesheets indicated that the AED purportedly worked at both United and Bushwick at virtually the same times each day.
- \$73,923 in retirement plan contributions that did not comply with RCM guidelines.
- \$52,304 in ineligible and/or undocumented OTPS costs, including: \$17,931 in inadequately supported vehicle-related costs; \$13,380 in costs for a car service to transport parents to United's main office; \$4,695 for food provided to staff; \$4,285 in utility expenses paid in lieu of rent associated with a studio apartment owned by United's Executive Director and Controller; and \$3,392 in unsupported cell phone costs, including the cell phone expenses of non-employees.

Unity House of Troy (Unity House) (2014-S-60) is a not-for-profit organization located in Troy, New York, that offers a variety of services to the community including preschool special education services to children with disabilities between the ages of three and five years. For the calendar year ending on December 31, 2012, Unity House reported approximately \$6.85 million in reimbursable costs for its preschool special education programs. The OSC audit recommended disallowances of \$404,952 in costs charged to the programs that did not comply with SED's requirements for reimbursement, including:

- \$312,543 in personal service and fringe benefit expenses that were overstated on the CFR;
- \$46,878 in OTPS costs that were incorrectly calculated and allocated;
- \$16,275 for gifts and food at restaurants and meetings that were either not allowed or not directly related to the preschool special education program; and
- \$13,653 for costs claimed from other programs operated by Unity House.

Whispering Pines Preschool, Inc. (Whispering Pines) (2013-S-48) is a for-profit organization that provides special education home-based and center services to infants, toddlers, and preschool-age children in nine counties in New York. For the two fiscal years ended June 30, 2012, Whispering Pines reported \$6.1 million in reimbursable costs for three rate-based programs. The OSC audit recommended disallowances of \$146,972 in disallowances that did not comply with SED's requirements for reimbursement, including:

- \$71,397 in personal service costs, consisting of salary and fringe benefits paid to the Director's husband and bonuses paid to some personnel that were not supported by performance evaluations; and
- \$75,575 in OTPS costs, including \$33,688 in ineligible or unnecessary vehicle and equipment costs and \$25,744 in ineligible interest expense.

In addition, the OSC audit noted that Whispering Pines did not disclose non-interest-bearing advances (totaling \$68,412) to its director that should have been reported on its CFRs as other compensation and benefits.

Whitestone School for Child Development (Whitestone) (2014-S-38) is a not-for-profit organization that provides pre-school special education services to children throughout Queens and neighboring boroughs. For the three fiscal years ended June 30, 2013, Whitestone reported \$6.2 million in reimbursable costs. The OSC audit recommended disallowances of \$154,563 in reported costs that did not comply with SED's requirements for reimbursement, including:

- \$58,355 in unsupported salary and fringe benefits for a part-time teacher's assistant who did not have standard work hours and who sometimes worked from home;
- \$56,941 in unsupported bonuses and associated payroll taxes; and
- \$39,267 in OTPS costs that were either unsupported, or were not eligible for reimbursement, including: \$16,243 in advertising expenses used to recruit students by offering free evaluation services; \$10,592 in unsupported vehicle expenses, including two vehicles used by one of the co-Executive Directors; and \$1,698 in personal expenses for staff/classroom parties and flowers.

Words 'N Motion Special Education Programs (Words 'N Motion) (2014-S-72) is a for-profit organization based in Staten Island, New York, that operates three SED-approved programs including preschool special education services to disabled children ages three through five years. For the three fiscal years ended June 30, 2013, Words 'N Motion reported approximately \$4.6 million in reimbursable costs for its preschool special education programs. The OSC audit recommended disallowances of \$135,174 in reported costs that did not comply with SED's requirements for reimbursement, including:

- \$62,895 in salary and related fringe benefits costs for six staff from another program that were incorrectly charged to the preschool special education program;

- \$32,770 in rent-related costs that were over-allocated to the special education program;
- \$19,827 in corporate taxes, advertising fees and other expenses that were ineligible for reimbursement; and
- \$17,787 in unsupported/ineligible staff development costs.

Yeled v'Yalda Early Childhood Center (Yeled) (2015-S-19) is a not-for-profit organization located in Brooklyn, New York, that offers a wide range of services that includes preschool special education programs to disabled children between the ages of three to five years. For the three fiscal years ended June 30, 2014, Yeled reported approximately \$81 million in reimbursable costs for its preschool special education program. The OSC audit scope period focused primarily on fiscal year 2013-14. However, OSC expanded its review to include certain items claimed on the CFRs for fiscal years 2011-12 and 2012-13. The OSC audit recommended disallowances of \$2,950,518 in costs reported that did not comply with SED's requirements for reimbursement, including:

- \$1,062,157 in OTPS costs related to non-approved SEIT sites. The ineligible costs include mortgage interest, depreciation, and other costs related to 20 sites that were not approved by SED.
- \$683,915 in OTPS costs from other programs that were incorrectly charged to the preschool special education program.
- \$571,929 in salaries and fringe benefits for employees who did not work for the preschool special education program.
- \$215,528 in over-allocated compensation paid to employees who were shared among multiple Yeled programs.
- \$74,025 in inadequately supported vehicle-related costs (including lease payments, insurance, maintenance, gas, penalties, and fees) charged to the program.
- \$104,282 in other various ineligible expenses, including \$62,645 for unsupported invoices, \$10,099 for unnecessary cell phone charges, and \$19,597 for gifts and flowers provided to employees and nonemployees.

Eight of the 23 preschool special education audits conducted during 2015 recommended 1.2 percent or less of claimed expenses be disallowed.

Astor Services for Children & Families (Astor) (2014S-66) is a not-for-profit organization located in Rhinebeck, New York, that offers a wide range of services and programs to children with disabilities between the ages of three and five years. Astor is also a SED-approved provider of a School Age Special Class program, and provides several other programs approved and funded by the State Office of Mental Health. For the fiscal year ended June 30, 2013, Astor reported \$6.4 million in reimbursable costs, of which \$3.3 million was for preschool special education programs. The OSC audit recommended disallowances of \$39,050 in non-reimbursable costs that did not comply with SED's requirements for reimbursement including, \$18,522 in expenses claimed from other programs and \$13,485 for non-reimbursable fundraising.

OSC's audit also identified two teachers and seven teacher's assistants who provided over 6,000 hours of instruction to students in the preschool special education program, but did not have the required certifications for their job titles.

Finger Lakes United Cerebral Palsy (Happiness House) (2015-S-10) is a not-for-profit organization located in the Finger Lakes Region of Central New York that provides preschool special education services to children with disabilities between the ages of three and five in Geneva, Canandaigua, and Waterloo, New York. For the fiscal year ended June 30, 2013, Happiness House reported about \$3.4 million in reimbursable costs on its CFR. The OSC audit recommended disallowances of \$15,454 in costs charged to the programs that did not comply with SED's requirements for reimbursement, including staff bonuses, travel expenses, and food and beverages provided to staff.

Just Kids Early Childhood Learning Center (Just Kids) (2015-S-13) is for-profit organization based in Middle Island, New York, that provides preschool special education services to disabled children between the ages of three and five years. Just Kids also operates a day care center and is affiliated with other entities. For the three fiscal years ending June 30, 2014, Just Kids reported approximately \$53.7 million in reimbursable costs for its preschool special education programs. The OSC audit recommended disallowances of \$417,994 in reported costs that did not comply with SED's requirements, including:

- \$148,590 for OTPS expenses claimed from another program;
- \$108,662 in employee daycare discounts given to employees who were not the parents of the students enrolled in their programs;
- \$70,951 for salary and fringe benefits claimed over three years for an employee who did not complete time and attendance records; and
- \$30,233 in consulting fees incorrectly allocated to the programs.

OSC's audit also identified two significant issues pertaining to related party (or LTAL) business arrangements, including lease agreements and contracted therapeutic services.

Newmeadow, Inc. (Newmeadow) (2015-S-48) is a non-profit organization located in Malta, New York, that offers a range of services and programs to children with disabilities from three to five years of age. For the fiscal year ended June 30, 2014, Newmeadow reported about \$2.9 million in reimbursable costs for three preschool special education programs. The OSC audit recommended disallowances of \$12,059 in costs charged to the programs that did not comply with SED's requirements for reimbursement, including \$3,897 in personal service costs, \$6,142 in costs associated with non-audit services provided by an accounting firm, and \$2,020 for food and gifts.

OSC's audit also determined that Newmeadow did not maintain sufficient inventory records or have a process for identifying board members' conflicts of interest on an ongoing basis.

Story Place Preschool, Inc. (Story Place) (2015-S-69) is a for-profit organization located in Castleton, New York, that offers a range of services and programs to children with disabilities. For the fiscal year ended June 30, 2014, Story Place reported \$1.9 million in reimbursable costs for its programs. The OSC audit recommended disallowances of \$5,150 in personal service costs that did not comply with SED's requirements for reimbursement.

Summit Educational Resources (Summit) (2014-S-49) is a not-for-profit organization located in Getzville, New York, that provides a wide range of services to children with disabilities from ages three through 21. For the fiscal year ended June 30, 2013, Summit reported about \$4.25 million in reimbursable costs for preschool special education programs. The OSC audit recommended disallowances of \$28,176 in OTPS costs charged to the programs that did not comply with SED's requirements for reimbursement, including \$26,754 for consultant services not supported by itemized invoices. OSC's audit also questioned the appropriateness of \$34,357 in costs charged to the programs for consultant services and information technology procurements not obtained through competitive bidding.

United Cerebral Palsy Association of the Rochester Area, Inc. (UCP Rochester) (2014-S-75) is a not-for-profit organization located in Rochester, New York, that provides preschool special education services to children with disabilities between the ages of three and five years. For the year ended December 31, 2013, UCP Rochester reported about \$1.7 million in reimbursable costs on its CFR for the preschool special education programs. The OSC audit recommended disallowance of \$6,634 in costs that did not comply with SED's requirements for reimbursement, including: \$2,210 in ineligible bonuses and associated fringe benefits; \$1,681 for inappropriate consultant services; and \$2,743 in OTPS costs that were either not allowed, not directly related to the preschool special education programs, or not properly documented.

Upstate Cerebral Palsy (Upstate) (2014-S-71) is a not-for-profit special education provider located in Utica, New York, that provides services to children with disabilities between the ages of three and five years. For the calendar year ended December 31, 2012, Upstate reported about \$7.9 million in reimbursable costs for three preschool special education programs. The OSC audit recommended disallowances of \$97,781 in costs reported by Upstate that did not comply with SED's requirements for reimbursements, including \$83,905 in personal service costs and \$13,876 in OTPS costs such as undocumented vehicle costs and ineligible food costs.

IMPACT OF AUDITS: AGENCY RESPONSES AND ACTIONS TAKEN

State Education Department

SED has reviewed the 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 measures 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 providers and 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 school year. SED’s objectives for the 2015-16 SEIS rates are: (1) account for a reasonable student absentee factor to be included in rates under a fee-for-service reimbursement methodology; (2) 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) 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. SED anticipates to have completed over 200 reapproval reviews of preschool special education providers by the conclusion of the 2015-16 school year.
- **Revised Approval Process for New Programs and Program Modifications** – SED has revised its special education provider approval application process to include an in-depth review of all program elements to ensure that high-quality services are delivered in an environment that protects the health and safety of students with disabilities, and that the provider has the appropriate background and qualifications to provide effective program and fiscal oversight. SED’s Preschool Unit within the Office of Special Education manages the provider application process, addresses preschool legislative and regulatory issues, provides policy guidance, provides technical assistance to providers and other external

parties, and coordinates efforts with other SED units to improve the oversight of preschool special education services.

- **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.
- **Review of Provider’s Approval Status Following Fiscal Audit** – SED has enhanced its criteria and developed a process for revocation of a provider’s approval based on fiscal concerns and/or misuse of public funds identified in audits; as a result, SED has taken action to terminate the approval of several preschool special education providers. In addition, several other providers were placed on conditional approval status, with full approval contingent upon submission of documentation to verify changes to their internal controls, governance and/or fiscal practices to address findings in the audits. For example, if an OSC audit identifies serious problems with a preschool special education provider’s methodology to allocate costs to the various programs which it operates, SED requires the provider to submit corrective action plans.
- **Strengthened Existing External Audit Requirement** – SED has enhanced its internal processes for referring CPAs to the Office of the Professions for professional misconduct based on substantial errors that are contained in a provider’s CFR that has been certified by a CPA, and in cases where an audit contains findings of potentially fraudulent spending or other intentional misuse of public funds. In March 2015, the SED’s Office of Professional Discipline’s Prosecutions Division notified OSC of actions taken by the Board of Regents against a CPA who was brought to their attention as a result of an OSC audit. The CPA pleaded guilty to a charge of unprofessional conduct for auditing errors, and agreed to a penalty of a partial suspension in the area of CFR auditing. The penalty included successful completion of continuing education credits (courses), followed by two years’ probation and a \$5,000 fine.
- **Revised SED Regulations** – To implement the provisions of Chapter 545 of the Laws of 2013, SED has enacted regulations to require that the executive director or person assigned to perform the duties of a chief executive officer hired or assigned on or after April 17, 2014, have a bachelor’s degree or higher in a field related to business, administration and/or education and that such individuals have knowledge and background regarding the program and supervisory requirements to: (1) operate a preschool special education program; (2) comply with applicable laws and regulations; (3) maintain or supervise the maintenance of financial and other records; (4) establish the approved program’s policy, program and budget; and (5) recruit, employ, train, direct and

evaluate qualified staff. In addition, the regulations require that all executive directors reside within a reasonable geographic distance from the program's administrative, instructional and/or evaluation sites to ensure appropriate oversight of the program. In addition, if paid as a full-time executive director, such individual must be employed in a full-time, full-year position and not engage in activity that would interfere with or impair the executive director's ability to carry out and perform his or her duties, responsibilities or obligations.

SED has proposed additional regulations relating to preschool providers that would clarify, consistent with State law, where SEIS can 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 proposed regulations would enhance 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.

RELATED AUDIT INITIATIVE

Services to New York's vulnerable populations are provided in large part through not-for-profit (NFP) providers that are funded by the Office of Mental Health (OMH), the Office of Alcohol and Substance Abuse Services (OASAS), and the Office for People with Developmental Disabilities (OPWDD). The State agencies either contract directly with the selected NFPs or provide funding to the counties, or to the New York City Department of Health and Mental Hygiene. As with the preschool special education providers funded by SED, NFP human services providers are required to report their expenses incurred and revenues received on CFRs submitted to the funding agencies. OSC's analysis of available CFR and other data showed that NFPs received more than \$13 billion in funding for the three years ended June 30, 2013.

Several recent audits (8) have identified NFP providers who reported expenses that were not allowable, not documented, or not program appropriate, and/or who overstated shared expenses and understated offsetting revenues. As with OSC audits of SED-funded preschool special education programs, OSC audits of contracts with NFP human services providers have identified weaknesses stemming from a lack of close monitoring and supervision by the oversight agencies, resulting in significant amounts of ineligible expenses being claimed by the NFPs. When considering the amount of State funds that these providers receive, the importance of the services they provide, and the identified weaknesses in the oversight of these NFPs it is clear that a concerted effort for change in this area is warranted.

CONCLUSION

As New York continues to strengthen its oversight of preschool special education programs, State policy makers must find ways 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, this Office will continue to promote best practices and to emphasize the importance of critical internal controls and responsible external oversight.

APPENDIX A

2015 OSC Special Education Program Audits

Provider	County	Audited Program Costs Reported on CFR	Number of Years in Scope	Total Disallowance
Astor Services for Children & Families	Dutchess	\$3,302,521	1	\$39,050
Clinical Associates of the Finger Lakes	Ontario	\$1,211,123	1	\$72,401
Finger Lakes United Cerebral Palsy	Ontario	\$3,369,638	1	\$15,454
Hear 2 Learn PLLC	Onondaga	\$340,876	1	\$20,851
Inspire (Orange County Cerebral Palsy Association)	Orange	\$6,446,254	1	\$226,382
Just Kids Early Childhood Learning Center	Suffolk	\$53,716,437	3	\$417,994
Kew Gardens SEP, Inc.	Queens	\$9,802,925	3	\$295,997
Kids-Centric, Inc.	Kings	\$14,197,592	3	\$301,601
Mid Island Therapy Associates, LLC	Nassau	\$10,577,085	3	\$655,055
Milestone School for Child Development	Kings	\$11,079,275	3	\$801,859
Newmeadow, Inc.	Saratoga	\$2,941,217	1	\$12,059
Rivendell School	Kings	\$7,449,096	3	\$536,449
Starting Point Services for Children	Kings	\$48,250,273	3	\$2,585,454
Story Place Preschool, Inc.	Rensselaer	\$1,872,436	1	\$5,150
Summit Educational Resources	Erie	\$4,254,210	1	\$28,176
United Community Services, Inc.	Kings	\$7,327,720	3	\$207,295
Unity House of Troy	Rensselaer	\$6,852,042	1	\$404,952
UPC of the Rochester Area, Inc.	Monroe	\$1,662,142	1	\$6,634
Upstate Cerebral Palsy	Oneida	\$7,949,919	1	\$97,781
Whispering Pines Preschool, Inc.	Montgomery	\$6,059,555	2	\$146,972
Whitestone School for Child Development	Queens	\$6,204,514	3	\$154,563
Words 'N Motion Special Education Programs	Richmond	\$4,606,987	3	\$135,174
Yeled v'Yalda Early Childhood Center	Kings	\$81,008,450	3	\$2,950,518
Total (23 providers)		\$300,482,287		\$10,117,821

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