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STATE OF NEW YORK
OFFICE OF THE STATE COMPTROLLER

September 12, 2016

Mr. Mitchell Hochberg
Chairman
Westchester County Health Care Corporation
100 Woods Road
Valhalla, NY 10595

Re: Supplemental Payments to Executive
Employees
Report 2015-S-77

Dear Mr. Hochberg:

Pursuant to the State Comptroller's authority as set forth in Article X, Section 5 of the State Constitution and Section 2803 of the Public Authorities Law, we audited the Westchester County Health Care Corporation – Supplemental Payments to Executive Employees. The audit covered January 1, 2012 to January 15, 2016.

Background

Westchester County Health Care Corporation (WCHCC) is a State Public Authority created under Sections 3300-3321 of the Public Authorities Law, with a 19-member Board of Directors consisting of 15 voting directors and four non-voting representatives that have all the rights and powers of voting directors other than the right and power to vote. Eight of the 15 voting directors are appointed by the Governor. It is responsible for governing the Westchester Medical Center. The primary mission of Westchester Medical Center is to serve as the regional healthcare referral center providing high-quality advanced health services to the residents of the Hudson Valley and the surrounding area. The Board is responsible for overseeing the actions of its Chief Executive Officer (CEO). The CEO is responsible for establishing policies related to the qualifications, duties, and payment of salaries and other compensation for all WCHCC executive employees.

Guidance regarding performance incentive programs for public authorities such as WCHCC has been developed through the application of two legal opinions issued by State oversight agencies. Specifically:

- In 2000, State Comptroller's Opinion #2000-9 was issued based upon a request for interpretation pertaining to a local industrial development agency (IDA). This Opinion

concluded that the IDA did not have statutory authority to make gifts to its officers and employees in the form of “after-the-fact” bonus payments, but that if the additional compensation was earned pursuant to a predetermined employee performance evaluation program, it would not constitute a gift; and

- Similarly, New York Attorney General Opinion 2007-F4 states that the ability to make gifts of assets would not directly relate to the powers, duties, or purposes of an authority. Further, an authority’s performance incentive compensation plan, where the benchmarks necessary to receive a bonus are established beforehand, was within the authority’s right to establish employee compensation levels.

As such, these Opinions provide that supplemental compensation payments (or bonuses) are allowable, if they correspond with pre-determined amounts paid after the end of pre-specified work periods for meeting certain performance criteria.

WCHCC reports various salary and compensation data through the Public Authorities Reporting Information System (PARIS), which is an online data entry and collection system maintained by the Office of the State Comptroller and managed jointly with the Authorities Budget Office (ABO). In 2012, WCHCC reported bonuses for 13 employees to the ABO. In 2013 and 2014, it reported bonuses for only two individuals.

Results of Audit

Supplemental Payments to Executive Employees

From 2013 through 2015, WCHCC paid 18 executives (with base salaries totaling about \$21.6 million) almost \$4.6 million in supplemental payments. The supplemental payments ranged from about \$20,000 to almost \$1.7 million per recipient for the three years ended December 31, 2014. In general, the supplemental payments corresponded to work performed during the previous year. The largest supplemental payments (totaling about \$2.7 million) were made to the CEO and the Chief Financial Officer (CFO) and accounted for almost 59 percent of the total paid. The other payments (totaling about \$1.9 million) were paid to members of “senior management,” which WCHCC defined as titles such as Senior Vice President and above.

Opinions of the State Comptroller and the Attorney General state that additional payments require the existence of an evaluation program with specific performance criteria set forth and disclosed prior to the performance of services, with a determination at the end of the period that the employee met the specified criteria and is eligible for the specified additional compensation. Both the CEO and the CFO had employment contracts with defined bonus clauses, including what they must do to earn the bonuses. Their performance is evaluated at the end of the year. However, the remaining executives (senior managers) did not have employment contracts with WCHCC, and thus, there were no specific criteria or benchmarks established upon which bonuses could be based.

Officials informed us that they do not refer to payments to senior management as bonuses, but instead consider them as “withholds,” or amounts withheld from base salary payments.

According to WCHCC officials, a “withhold” typically represents about 10 to 20 percent of a senior manager’s base pay that is paid in a lump sum amount in the following year. We determined, however, that the lump sum payments of the amounts withheld actually ranged from 3 percent to 26 percent of employees’ base salaries.

Further, when we reviewed the payroll records for senior managers, we found no evidence of any amounts withheld for the reasons cited by WCHCC officials. According to officials, information pertaining to amounts of base compensation withheld is not reflected on the payroll. Nevertheless, when we examined one employment offer letter for a senior management position during our audit period, we found the individual was offered a specific base pay, and the position was subject to a “Bonus Program.” Further, there were no provisions for amounts of withheld compensation for the position. In fact, the CEO, CFO, and the other members of senior management received their full base pay over 12 months and supplemental payments (in addition to their base pay). WCHCC officials stated that all payments were made to employees for meeting performance expectations. Moreover, based on the results of our review, we concluded that the payments in question were supplemental payments, rather than portions of the senior managers’ base compensation that were withheld.

WCHCC officials stated that senior management had goals and were evaluated on achieving those goals before receiving their payments. Officials added, while they do not have a formal evaluation process for senior management, the CEO meets with all the senior executives each December to discuss their submitted goals and objectives for the following year as well as his expectations. At the end of the period, the CEO evaluates the CFO’s as well as each senior manager’s performance. The CEO stated that this process is flexible because priorities change from day to day, and to evaluate against a fixed set of goals created in the beginning of the year would not be objective. The CEO, who is evaluated by the Board, added that his bonus is dependent upon achieving goals set by the Board.

When we reviewed the documents provided by WCHCC, we found that 7 of the 14 senior managers submitted both Goals and Achievements in 2012. Thereafter, the number of employees submitting both documents fell, and in 2014, only 2 of the 14 did so. None of the employees submitted both documents in all three years. (Note: Two senior managers were not employed until May and August of 2014, respectively, and therefore, they did not have to prepare the Achievement documents at the time of our review.) Further, WCHCC officials could not provide us with written performance evaluations for any senior managers.

In response to our preliminary findings, WCHCC officials restated their views that the supplemental payments were not bonuses, but part of the “total compensation withhold” process. Nevertheless, they added that “commencing in 2016, WCHCC will no longer compensate the members of senior management by utilizing a ‘total compensation withhold’ process. Instead, they will be paid an annual salary, in full, and be eligible to receive a bonus payment provided they have met articulated, measurable goals above and beyond meeting the expectations for their positions, as determined and documented on an annual basis by the CEO.” We believe such actions, if taken, will strengthen the controls over and increase the propriety of supplemental (or bonus) payments to senior WCHCC management.

We also identified other payments which we believe require further examination by WCHCC officials. Specifically, we questioned:

- A \$20,000 payment to an employee in 2013 for “extraordinary performance.” We were provided with no documentation to show what this performance consisted of or how it fit in with WCHCC’s practices. It is, therefore, unclear how this payment met any of the criteria for additional payments;
- A payment to an employee in 2013, who was eligible for a 10 percent payment. This employee was paid only 3 percent of the payment for which he was eligible. However, in the next year, he was paid the remaining 7 percent. We were informed that a decision to pay the remaining amount was based on the employee’s improved performance. Nonetheless, based on the current guidance, it is unclear if such amendments to agreements for additional payments are permissible after the fact;
- A sign-on bonus (totaling \$10,000) paid to a senior manager in 2014. We question this payment because it is not based on performance or part of an employee’s regular compensation for work performed; and
- Retention bonuses (totaling \$1,343,652) paid to the CEO and CFO as part of their employment agreements. We question WCHCC’s authority to agree to such terms since the payments were not predicated on the accomplishment of specific performance criteria, including prescribed benchmarks.

Reports to the State Authorities Budget Office

Pursuant to the Public Authorities Law, Section 2800-1(a)(5), state authorities are required to report annually to the ABO the salary, compensation, allowance, and/or benefits paid to employees in decision-making or managerial positions whose salary is in excess of \$100,000.

In its 2012 report to the ABO, WCHCC listed bonuses (totaling \$940,338) paid to 13 employees, including the CEO and CFO. However, for 2013 and 2014, WCHCC reported bonuses (totaling \$634,663 in 2013 and \$530,098 in 2014) for only two employees, the CEO and CFO. Further, when we reviewed payroll records, we found WCHCC made supplemental payments to members of senior management throughout the period. In all, from 2013 through 2015, supplemental payments were made to 18 employees, including the CEO, CFO, and 16 other senior managers, for job performance during the 2012-14 period. When we questioned the reporting inconsistency, WCHCC officials told us that the payments to senior managers made in 2014 and 2015 (for the 2013 and 2014 years) were not bonuses. Rather, according to officials, the payments were part of the senior managers’ total compensation, part of which was withheld pending satisfactory completion of their duties.

In response to our preliminary findings, WCHCC officials acknowledged that their ABO reports for 2012 through 2014 were inconsistent. Officials also indicated, however, that the ABO’s compensation reporting system differs from the manner in which WCHCC compensates its senior managers (other than the CEO and CFO) because it does not include a category for “withheld compensation.” Officials added that this incompatibility led to the inconsistencies in

WCHCC's reporting for those years. Nevertheless, as stated previously, we found no evidence of any withheld compensation. Further, a recent letter offering a position to a senior manager made no reference to withheld compensation, but referenced the position's eligibility for WCHCC's "Bonus Program."

As previously stated, WCHCC indicated it will change its compensation process for senior management. According to WCHCC officials, "This change also will simplify WCHCC's ABO reporting process and ensure consistency between the reporting for the CEO and COO/CFO and the other members of our senior management."

Recommendations

1. Establish and document a formal program for the award and payment of supplemental executive payments, which complies with the opinions of the State Comptroller and Attorney General. In particular, the program should ensure that: specific performance criteria is established and disclosed prior to the performance of services; and payments are made after the end of the period and only upon formal determination that an employee has met the prescribed criteria.
2. Determine whether the following payments made by WCHCC comply with the opinions of the State Comptroller and the Attorney General:
 - Offering and paying hiring sign-on bonuses to employees for accepting positions at WCHCC;
 - Offering and paying retention bonuses, for the purposes of inducing personnel to remain in WCHCC's employ;
 - Making supplemental payments to employees, outside of a formal bonus program, based on performance; and
 - Amending employment agreements for additional compensation payments after the period of employment in question has begun.
3. Ensure that all reports to the ABO/PARIS contain complete and accurate data.

Audit Scope, Objectives and Methodology

The objectives of our audit were to determine whether WCHCC has a formal supplemental compensation program and whether the payments under the program were warranted and justified. The audit covered the period January 1, 2012 through January 15, 2016, and focused on payments to senior management employees for their performance during calendar years 2012 through 2014.

To accomplish our objectives, we met with WCHCC officials to gain an understanding of the internal controls related to the supplemental payments to senior management. We reviewed payroll records for all 18 senior management employees, the contracts between the WCHCC and the CEO and CFO, reports to the ABO, minutes of the WCHCC Board as related to compensation and goal plans, and end-of-year accomplishments for senior management. We also reviewed

offer letters sent to applicants for senior management positions at the WCHCC.

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 objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

In addition to being the State Auditor, the Comptroller performs certain other constitutionally and statutorily mandated duties as the chief fiscal officer of New York State. These include operating the State's accounting system; preparing the State's financial statements; and approving State contracts, refunds, and other payments. In addition, the Comptroller appoints members to certain boards, commissions, and public authorities, some of whom have minority voting rights. These duties may be considered management functions for purposes of evaluating organizational independence under generally accepted government auditing standards. In our opinion, these functions do not affect our ability to conduct independent audits of program performance.

Reporting Requirements

We provided a draft copy of this report to WCHCC officials for their review and formal comment. Their comments were considered in preparing this final report and are attached in their entirety at the end of this report. In their response, WCHCC officials maintain their position that its compensation program for executive employees was appropriate. Our rejoinders to certain WCHCC comments are included in this report's State Comptroller's Comments.

Within 90 days after the final release of this report, as required by Section 170 of the Executive Law, the Chairman of the Westchester County Health Care Corporation 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 the recommendations were not implemented, the reasons why.

Major contributors to this report were Robert C. Mehrhoff, Erica Zawrotniak, Richard Moriarty, and Elijah Kim.

We wish to thank the management and staff of the Westchester County Health Care Corporation for the courtesy and cooperation extended to our auditors during this audit.

Very truly yours,

Carmen Maldonado
Audit Director

cc: J. Switzer, WCHCC
NYS Division of the Budget

Agency Comments



Julie Switzer
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June 20, 2016

Via EMAIL and FEDEX

Carmen Maldonado
Audit Director
Office of the State Comptroller
Department of State Government Accountability
59 Maiden Lane, 21st Floor
New York, NY 10038

Re: Westchester County Health Care Corporation
Draft Audit Report 2015-S-77

Dear Ms. Maldonado:

Enclosed please find Westchester County Health Care Corporation's ("WCHCC") response to the OSC's Draft Audit Report 2015-S-77.

We greatly appreciate the opportunity to provide this response to you and hope the OSC will take into account the points made in WCHCC's response as it prepares its final report.

Thank you.

Very truly yours,

Julie Switzer

JS:tt

cc: Mitchell Hochberg, Chair, WCHCC Board of Directors
Michael D. Israel, President & CEO, WCHCC

**WESTCHESTER COUNTY HEALTH CARE CORPORATION
RESPONSE TO THE OFFICE OF THE STATE COMPTROLLER'S
DRAFT REPORT RE: SUPPLEMENTAL
PAYMENTS TO EXECUTIVE EMPLOYEES**

On May 20, 2016, the Office of the State Comptroller ("OSC") forwarded its Draft Report to the Westchester County Health Care Corporation regarding its audit of WCHCC re: Supplemental Payments to Executive Employees. This Response will address, in the order in which they appear, each of the OSC's findings in the Draft Report.

WCHCC is confident that the characteristics of its incentive compensation program for its executive employees, who are defined as members of management at the level of Senior Vice President and above, were consistent with the principles of a sound incentive compensation program during the four (4) year period that was the subject of the OSC audit.

Background

WCHCC would like to correct a few matters set forth in the Background section of the OSC's Draft Report. First, the Draft Report states that WCHCC has a fifteen (15) member Board of Directors. In fact, WCHCC's Board of Directors consists of fifteen (15) voting directors and four (4) non-voting directors, for a total of nineteen (19) directors.

Second, the Board of Directors is a governing body, not a managing body. Contrary to the OSC's statement in the Draft Report, the President and Chief Executive Officer ("CEO"), not the Board, is charged with managing WCHCC. The CEO's performance is overseen by the Board of Directors.

Lastly, neither the section of the Public Authorities Law that created WCHCC, nor WCHCC's corporate bylaws, provides that the Board of Directors is charged with "establishing policies related to the qualifications and duties and other compensation for all WCHCC executive employees" as the Draft Report states. On the contrary, such matters are wholly within the purview of the CEO. In fact, the Public Authorities Law only states that "the voting directors shall select and shall determine the salary and benefits of the Chief Executive Officer," and the corporate bylaws provide only that the Personnel and Compensation Committee of the Board "recommend to the Board . . . compensation levels for the President and CEO and CFO" and "review the President and CEO's decisions with respect to the salaries, pay at-risk determinations and other compensation for all eligible staff at the level of Executive Vice President and above. . ." It should be noted that the term "pay-at-risk" in the corporate bylaws is specifically referring to WCHCC's salary withhold program.

However, as WCHCC's governing body, the Board of Directors has adopted policies regarding the parameters of the total compensation program for its executive employees, including the "pay-at-risk" or "salary withhold" component. Such policies are, and have always been, strictly adhered to throughout the period that was the subject of the OSC's audit.

* Comment 1

*See State Comptroller's Comments, page 13.

WCHCC acknowledges that the guidances upon which the OSC relies state that supplemental compensation payments are allowable if paid to employees after the end of pre-specified work periods and correspond to such employees' meeting certain performance criteria. As discussed below, WCHCC maintains that WCHCC's annual supplemental payments to its executive employees during the period that was the subject of the OSC audit were made in accordance with its total compensation program and incentive compensation/salary withhold process and met the recommendations in the guidances relied upon by the OSC, as such payments were made after pre-specified work periods and corresponded to the employees' meeting certain performance criteria.

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Comment
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With respect to the two isolated instances of supplemental payments to employees cited in the Draft Report that fell outside the salary withhold process, such payments were nominal and, when added to each individual's base salary, did not alter the fact that their total compensation amount for that year remained within the Board-approved parameters of a reasonable annual total compensation amount for each such position.

Results of Audit

Supplemental Payments to Executive Employees

WCHCC would first like to address the statement in the Draft Report that supplemental payments to members of senior management ranged from "about \$20,000 to almost \$1.7 million per recipient". This statement is misleading, as the inference is that one individual received \$1.7 million (or something near that amount) in a given year for work performed in the previous year. That is not the case, and if the OSC is looking at cumulative amounts over the four year audit period, we would request that the Draft Report state that more clearly.

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Comment
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WCHCC also takes issue with the OSC's position that because no executive employees other than the CEO and CFO had employment contracts, there were no criteria upon which supplemental payments to such employees during the period that was the subject of the audit could be based. As was discussed at great length on site with the auditors and supported by ample documentation provided to them, members of senior management submitted to the CEO their Goals for the coming year on an annual basis and, at the end of such year, they submitted their Accomplishments. WCHCC respectfully disagrees with the OSC's position that few Goals and Accomplishments documents were submitted by members of senior management during the period that was the subject of the audit.*

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Comment
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WCHCC appreciates that its "salary withhold program" is less straight-forward than a simple bonus program. With that in mind, WCHCC believes that the OSC continues to have misconceptions about WCHCC's salary withhold process as a component of its total compensation program. Such misconceptions, WCHCC maintains, appear to form the basis of

*As was pointed out in WCHCC's May 9, 2016, Response to the Preliminary Audit Report, some individuals submitted such documentation to the CEO through the person to whom they report, who then submitted those Goals and Accomplishments as a subset of theirs. Specific examples of this practice were included in WCHCC's Response.

the OSC's position that the executive employees who received salary withhold payments as incentive compensation during the period that was the subject of the audit did not receive such payments in accordance with the guidances upon which the OSC relies. However, consistent with the guidances, salary withhold payments are and always have been incentive payments paid to executive employees after the end of pre-specified work periods, and they correspond to determinations by the CEO that each such employee met certain expected performance criteria. To reiterate the points WCHCC made in its March 9, 2016, Response to the OSC's Preliminary Audit Report, and consistent with the written policy of the Board of Directors, WCHCC compensates its executive employees on a "total compensation" basis; i.e., a total compensation amount for each person is set by the CEO annually, and a portion of such amount is withheld (or "at risk") until the following year after the CEO reviews the employee's Accomplishments for the prior year and determines whether such employee performed his or her duties consistent with the Goals submitted to the CEO for that year. Accordingly, a payment is paid to a member of senior management only if the CEO determines he or she has met the expectations of his or her position and, unlike a bonus, it is not a payment for doing more than the position requires. WCHCC maintains that these withheld or, at-risk, payments are incentive payments, as executive employees whom the CEO deems did not perform as expected would not receive such payments the following year.*

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Comment
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Comment
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Comment
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The fact that the payroll records of executive employees did not reflect the amounts withheld from their total compensation amounts is not dispositive of the OSC's claim that the amounts were not in fact withheld. An executive employee's bi-weekly paycheck will equal 1/26 of that employee's total compensation amount for that year, as set by the CEO, minus the percentage of the total compensation amount withheld. The parameters of those percentage amounts, or "at-risk" amounts, as set forth in the corporate bylaws, were also established by the Board.

However, as WCHCC first advised the OSC in its March 9, 2016, Response to the Preliminary Audit Report, as a result of the inherent complexity in both the auditing process and ABO reporting of such incentive payments, commencing in calendar year 2016, WCHCC will move to a bonus program for its executive employees and will eliminate the salary withhold process. In addition, WCHCC will ensure that there is more robust documentation of the executive employees' annual performance appraisals.

Reports to the State Authorities Budget Office

As stated in WCHCC's March 9, 2016, Response to the Preliminary Audit Report, the nature of the salary withhold process and its incompatibility with the mandatory ABO reporting forms led to some confusion in some of WCHCC's reporting to the ABO during the period that was the subject of the audit. WCHCC is confident that the reporting errors that resulted from

* WCHCC does acknowledge that although the CEO annually reviewed the performance of each member of senior management who was eligible to receive incentive compensation, WCHCC did not provide the OSC with written performance evaluations prepared by the CEO.

such confusion will not recur as it replaces the salary withhold process with a bonus program for its executive employees.

WCHCC does take exception, however, with the OSC's statement that they "found no evidence of any withheld compensation." As stated previously in this Response, and on many other occasions and in other written submissions, the incentive compensation process in place at WCHCC for its executive employees since 2012 has unequivocally been in the form of a total compensation program with a salary withhold component. The Board of Directors' policies that outline this process were provided to the auditors. The fact that it is not evident in the bi-weekly payroll records, but is only evidenced in documentation of the executive's cumulative payroll data at year end, does not make it any less true.

Conclusion

WCHCC maintains that its total compensation approach and salary withhold process are consistent with the incentive compensation guidelines set forth in the guidances upon which the OSC relies. Although the process differs from a bonus program, in that such incentive payments are tied to a percentage of an executive employee's total compensation amount for a given year that has been withheld, and are only paid out to employees who meet the expectations of their position, as opposed to extra dollars paid to reward a person for going above and beyond what is expected of them, does not mitigate that fact.

Finally, WCHCC is replacing its salary withhold process for its executive employees with an annual bonus program commencing in 2016. WCHCC is confident that such annual bonus program will meet the expectations of the OSC.

Thank you.

State Comptroller's Comments

1. We revised our final report, as appropriate, based on WCHCC's response to our draft report.
2. Despite WCHCC's assertion that payments were made after pre-specified work periods and corresponded to the employees meeting certain performance criteria (per the Goals document and the Accomplishments document), none of the 14 senior managers submitted both documents in all three years, as detailed in the report. In addition, WCHCC officials did not provide written performance evaluations for any senior managers, as also detailed in the report.
3. As noted previously, none of the 14 senior managers submitted both Goals and Accomplishments documents in all three years. In 2014, for example, only 2 of the 14 submitted both. In addition, WCHCC officials did not provide written performance evaluations for any senior managers.
4. The totality of the evidence, including our review of payroll records and employment offer letters for the period under audit, refutes WCHCC's position.
5. We recognize that payroll records alone may not reflect amounts of compensation withheld (assuming amounts are withheld). Consequently, in addition to payroll records, we reviewed other records (including job offer letters), during our audit period. We noted that an offer letter for a senior management position provided a defined base compensation and also specifically stated that the position was subject to a "Bonus Program." Further, there was absolutely no mention of a "withhold" or a "total compensation" program. Moreover, this individual (who WCHCC hired) received similar treatment for supplemental payments as other senior managers who were also covered by WCHCC's "total compensation" program.