



Commonwealth of Massachusetts
Office of the State Auditor
Suzanne M. Bump

Making government work better

Issued Audit Report – May 25, 2021

Berkshire County Arc, Inc.

For the period July 1, 2017 through June 30, 2019





Commonwealth of Massachusetts
Office of the State Auditor
Suzanne M. Bump

Making government work better

May 25, 2021

Mr. Michael Ferry, Chair of the Board of Directors
Berkshire County Arc, Inc.
395 South Street
Pittsfield, MA 01201

Dear Mr. Ferry:

I am pleased to provide this performance audit of Berkshire County Arc, Inc. This report details the audit objectives, scope, methodology, findings, and recommendations for the audit period, July 1, 2017 through June 30, 2019. My audit staff discussed the contents of this report with management of the agency, whose comments are reflected in this report.

I would also like to express my appreciation to Berkshire County Arc, Inc. for the cooperation and assistance provided to my staff during the audit.

Sincerely,

A handwritten signature in blue ink, appearing to read "SMB", written over a light blue circular watermark.

Suzanne M. Bump
Auditor of the Commonwealth

cc: Mr. Kenneth Singer, President and Chief Executive Officer, Berkshire County Arc, Inc.
Mr. Gary Lambert, Assistant Secretary for Operational Services, Operational Services Division
Ms. Jane Ryder, Commissioner, Department of Developmental Services

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LIST OF ABBREVIATIONS

BCArc	Berkshire County Arc, Inc.
CEO	chief executive officer
CMR	Code of Massachusetts Regulations
COO	chief operating officer
CPS	Complete Payroll Solutions
ETS	Economized Time Services
GAAP	generally accepted accounting principles
ID	identification
OSA	Office of the State Auditor
OSD	Operational Services Division
UFR	Uniform Financial Statement and Independent Auditor's Report

EXECUTIVE SUMMARY

In accordance with Section 12 of Chapter 11 of the Massachusetts General Laws, the Office of the State Auditor (OSA) has conducted a performance audit of Berkshire County Arc, Inc. (BCArc) for the period July 1, 2017 through June 30, 2019. The purpose of this audit was to determine whether (1) BCARC’s management staff members were fully qualified for their positions and the compensation BCARC provided to them was allowable according to BCARC’s policies and procedures and Section 1.05(24) of Title 808 of the Code of Massachusetts Regulations (CMR); (2) BCARC’s credit card expenditures were documented and allowable in accordance with its policies and procedures and 808 CMR 1.04(1), 1.04(5), 1.05(3), 1.05(9), 1.05(10), 1.05(12), 1.05(23), and 1.05(26); and (3) BCARC conducted its related-party transactions¹ in accordance with 808 CMR 1.05(8) and 1.05(12).

This audit was conducted as part of OSA’s ongoing efforts to audit human service contracting activity by state agencies and to promote accountability, transparency, and cost-effectiveness in state contracting.

Below is a summary of our findings and recommendations, with links to each page listed.

Finding 1a Page 16	BCARC charged \$124,247 in nonreimbursable expenses to its state contracts.
Finding 1b Page 21	BCARC’s president and chief executive officer (CEO) used agency credit card reward travel miles for his personal travel.
Finding 1c Page 24	BCARC did not properly administer its inventory of non–generally accepted accounting principles (GAAP) fixed assets.

1. Related-party transactions can involve various parties, such as individuals, their family members, organizations, and trusts. According to the Financial Accounting Standards Board’s “Statement of Financial Accounting Standards No. 57,” a party “is a related party if it can significantly influence the management or operating policies of the transacting parties or if it has an ownership interest in one of the transacting parties and can significantly influence the other to an extent that one or more of the transacting parties might be prevented from fully pursuing its own separate interests.”

<p>Recommendations Page <u>25</u></p>	<ol style="list-style-type: none"> 1. BCARC should cooperate with the state Operational Services Division (OSD)² and determine how much of this \$124,247 of nonreimbursable credit card expenses BCARC should reimburse to the Commonwealth. 2. BCARC should amend its policies and procedures to ensure that all credit card expenses are properly documented according to OSD regulations. 3. BCARC management should establish monitoring controls to ensure that management reviews all credit card expenses before payment and determines whether they are reimbursable to BCARC’s state contracts. 4. BCARC should properly identify and correctly report all nonreimbursable expenses on its Uniform Financial Statements and Independent Auditor’s Reports. 5. BCARC should stop using the American Express and Citibank cards that are linked to the president and CEO’s account and obtain new cards issued in its own name. 6. BCARC should enhance its policies and procedures to require that all cards be issued in its name and that any travel rewards or other incentives issued by card companies be used solely for its benefit. 7. BCARC’s board should provide effective oversight over cards by periodically reviewing card statements to determine whether rewards are earned and how they are used. 8. BCARC should develop policies and procedures for the administration of its non-GAAP fixed assets that include a requirement that its inventory records contain all key information and be maintained and current for each asset as suggested in the “Fixed Assets—Acquisition Policy.”
<p>Finding 2 Page <u>26</u></p>	<p>BCARC charged at least \$651,540 in unallowable related-party expenses against its state contracts.</p>
<p>Recommendations Page <u>28</u></p>	<ol style="list-style-type: none"> 1. BCARC should cooperate with OSD to resolve any identified issues regarding nonreimbursable costs and should reimburse the Commonwealth for any such costs that OSD determines must be repaid. 2. BCARC should perform a fair market rent determination for the properties it leases from Berkshire Omega annually and use this information to determine what rents it should pay Berkshire Omega for these properties (i.e., the lower of the fair market rent or Berkshire Omega’s actual costs related to the properties). 3. BCARC should stop using state funds to pay for any capital improvements to Berkshire Omega’s properties and should enter into repayment agreements with Berkshire Omega for the capital improvements for which it has already paid. 4. BCARC should not pay for the maintenance of Berkshire Omega’s properties or its bookkeeping expenses.

2. OSD is the state agency responsible for regulating and overseeing the activities of all the state’s contracted human service providers, such as BCARC.

Finding 3 Page <u>30</u>	BCArc allowed inappropriate use of its credit cards.
Recommendations Page <u>31</u>	<ol style="list-style-type: none">1. BCArc should amend its credit card policies to limit card use to employees and establish monitoring controls to ensure that all employees and contractors comply with this requirement.2. BCArc should improve its internal controls over credit cards to prevent the cards from providing a personal benefit to anyone.
Finding 4 Page <u>32</u>	BCArc did not have required documentation for \$43,192 in client fund expenditures.
Recommendation Page <u>32</u>	BCArc should develop procedures to monitor the use of client funds to ensure that all expenses paid for with these funds are properly approved using the Savings Withdrawal Form.

Post-Audit Action

BCArc’s board of directors indicated that as a result of the problems identified in Finding 1b, the agency had implemented a new credit card policy prohibiting any employee from deriving a personal benefit from an agency credit card.

OVERVIEW OF AUDITED ENTITY

Berkshire County Arc, Inc. (BCArc), located in Pittsfield, was incorporated on February 2, 1959 under Chapter 180 of the Massachusetts General Laws as a nonprofit human service agency. During our audit period, BCARC provided residential and support services to individuals with developmental disabilities, brain injuries, and autism, as well as individuals who need help with activities of daily living at home. A detailed description of the programs BCARC operated during our audit period appears in the [Appendix](#) to this report.

During fiscal years 2018 and 2019, BCARC received revenue from the following sources.

Summary of Revenue³

Revenue Source	Fiscal Year 2018	Fiscal Year 2019
Department of Developmental Services	\$ 20,101,087	\$ 21,427,435
Massachusetts Rehabilitation Commission	3,885,564	3,949,255
Medicaid—Direct Payment	5,697,253	5,856,634
Commercial Activities	3,303,522	3,135,274
Client Resources	1,441,144	1,506,194
Other Grant	30,000	32,000
Massachusetts Commission for the Blind	10,173	11,922
Department of Children and Families	17,966	–
Private Client Fees (Excluding Third-Party)	13,826	277,288
Private Client / Third-Party / Other Offsets	201,215	49,712
Government In-Kind/Capital Budget*	26,640	50,579
Private In-Kind	230,394	232,632
Federated Fundraising	3,079	2,825
Contributions, Gifts, Legacies, and Bequests	95,836	145,585
Investments	131,380	96,466

3. This information was extracted from the Uniform Financial Statements and Independent Auditor's Reports that BCARC filed with the Commonwealth. Under the state Operational Services Division's regulations (Section 1 of Title of 808 of the Code of Massachusetts Regulations), any contractor or subcontractor that has been awarded a contract to provide human and/or social services from a Commonwealth agency is required to file this report, properly completed, each year. It contains contractual and financial information prescribed by the Operational Services Division, including audited basic financial statements.

Revenue Source	Fiscal Year 2018	Fiscal Year 2019
Other Revenue	419,206	398,029
Released Net Asset—Program†	65,693	1,155
Total	<u>\$ 35,673,978</u>	<u>\$ 37,172,985</u>

* The state Operational Services Division (OSD), in its *UFR Audit & Preparation Manual*, defines government in-kind/capital revenue as “the imputed revenue value of donated goods and personal services.”

† Released net assets are donated assets that have become available for spending because a donor-imposed stipulation has been satisfied.

BCArc Credit Cards

During our audit period, BCARC purchased \$800,698 worth of goods and services using 51 agency credit cards:

- Citi CitiBusiness/AAdvantage Platinum Select: 10 credit cards; total charges of \$615,424
- American Express: 3 credit cards; total charges of \$18,881
- Home Depot: 10 credit cards; total charges of \$64,006
- Walmart: 11 credit cards; total charges of \$48,642
- ExxonMobil: 7 credit cards; total charges of \$38,353
- Staples: 2 credit cards; total charges of \$12,044
- Big Y: 5 credit cards; total charges of \$3,348
- Best Buy: 2 credit cards; total charges of \$0⁴
- Sears: 1 credit card; total charges of \$0

BCARC policies state that BCARC’s president and chief executive officer (CEO) approves the issuance of credit cards to employees. During our audit period, 25 BCARC employees were issued BCARC credit cards with authorized credit limits ranging from \$3,000 to \$46,800 per card; some employees were issued more than one card. If an employee does not have an assigned credit card but wants to use one, s/he must complete a purchase order form that includes supervisor approval. The employee then signs out the credit card from BCARC’s Accounting Department and must return it to the Accounting Department with a receipt for the purchase within 24 hours.

4. According to BCARC’s vice president of finance, the Best Buy and Sears credit cards were not used during the audit period because the stores had closed.

Related-Party Organizations

During our audit period, BCARC conducted business with six related-party organizations. OSD has promulgated regulations regarding related-party transactions; Section 1.02 of Title 808 of the Code of Massachusetts Regulations defines “related party” as “any person or organization satisfying the criteria for a Related Party published by the Financial Accounting Standards Board in Statement of Financial Accounting Standards No. 57.”

“Statement of Financial Accounting Standards No. 57” defines “related parties” as follows:

Affiliates of the enterprise; entities for which investments are accounted for by the equity method by the enterprise; trusts for the benefit of employees, such as pension and profit-sharing trusts that are managed by or under the trusteeship of management; principal owners of the enterprise; its management; members of the immediate families of principal owners of the enterprise and its management; and other parties with which the enterprise may deal if one party controls or can significantly influence the management or operating policies of the other to an extent that one of the transacting parties might be prevented from fully pursuing its own separate interests. Another party also is a related party if it can significantly influence the management or operating policies of the transacting parties or if it has an ownership interest in one of the transacting parties and can significantly influence the other to an extent that one or more of the transacting parties might be prevented from fully pursuing its own separate interests.

The following are the related-party organizations with which BCARC conducted business during our audit period.

1. Berkshire Omega

Berkshire Omega, which is located at the same address as BCARC in Pittsfield, was incorporated on June 26, 1980, under Chapter 180 of the General Laws, as a nonprofit corporation. Berkshire Omega’s board of directors has five members who are appointed by BCARC’s board of directors. According to Berkshire Omega’s articles of incorporation, Berkshire Omega operates solely and exclusively for the benefit of BCARC. Berkshire Omega purchases residential and commercial real estate and then, as detailed in the “BCARC Property Lease Information” table below, leases them to BCARC, which uses them to house its programs. BCARC performs all of Berkshire Omega’s recordkeeping and accounting and performs maintenance at Berkshire Omega’s properties. It also finances all the capital improvements made to Berkshire Omega’s properties. BCARC has guaranteed Berkshire Omega’s outstanding debt on a number of its properties; the outstanding debts are outlined in the “Berkshire Omega Debt Guaranteed by

BCArc" table below. If Berkshire Omega becomes unable to make its mortgage payments on these properties when they are due, BCARC is contractually obligated to make the payments and is entitled to take ownership of the properties.

BCArc Property Lease Information

Property/Location	Rent Amount Fiscal Year 2018	Rent Amount Fiscal Year 2019
395 South Street, Pittsfield*	\$ 37,686	\$ 38,583
374 South Street, Pittsfield	3,926	3,924
36 Superior Street, Pittsfield	1,206	870
Swamp Road, Richmond	17,734	17,151
69 Onota Street, Pittsfield	3,222	3,162
1531 West Street, Pittsfield	6,878	6,543
814 North Street, Pittsfield	1,851	1,809
379 Elm Street, Pittsfield	1,607	2,541
288 Pecks Road, Pittsfield	3,538	3,291
490 South Main Street, Lanesborough	16,282	15,768
123 Wealthy Avenue, Pittsfield	419	1,452
979 Dalton Avenue, Pittsfield	22,661	22,395
70 Sampson Avenue, Pittsfield	9,633	9,198
20 Taconic Park Drive, Pittsfield	36,406	36,030
Quarry Hill Road, Lee	119,177	116,193
61-71 Depot Street, Dalton	61,633	59,949
10 Wyantenuck Street, Housatonic	20,798	20,574
North Main Street, Lanesborough	33,902	32,784
Sammy Lane, Westfield	31,957	30,672
North Road, Westfield	38,684	37,662
Woodland Road, Westfield	25,423	23,196
Morgan Road, West Springfield	34,820	33,708
Valentine Road, Pittsfield	39,064	41,277
Dug Road, Westfield	47,401	45,678
Coleman Road, Southampton	43,898	39,384
Sheep Pasture (Edgewood), Southwick	48,530	42,666
College Highway, Southampton	53,965	43,440

Property/Location	Rent Amount Fiscal Year 2018	Rent Amount Fiscal Year 2019
Ann Drive, Pittsfield	24,370	24,075
East Housatonic, Dalton	44,586	52,608
Old Cheshire Road, Lanesborough	–	37,562
Total	<u>\$ 831,257</u>	<u>\$ 844,145</u>

* This property address is the headquarters of both Berkshire Omega and BCArc.

Berkshire Omega Debt Guaranteed by BCArc

Property	Balance on June 30, 2018	Balance on June 30, 2019
Coleman Road, Southampton	\$ 260,750	\$ 254,910
Sheep Pasture (Edgewood), Southwick	283,640	277,287
61–71 Depot Street, Dalton	374,788	326,627
North Road, Westfield, and North Main Street, Lanesborough	704,632	663,587
College Highway, Southampton	558,141	201,732
East Housatonic, Dalton	652,380	393,268
Ann Drive, Pittsfield	243,204	237,711
Old Cheshire Road, Lanesborough	379,168	622,298
Nicholson Hill	–	542,833
Kosak Court	–	313,745
Total	<u>\$ 3,456,703</u>	<u>\$ 3,833,998</u>

2. Berkshire Community Apartments, Inc.; Hollow Road Development Corporation; Lanesboro Development Corporation; and Gamwell Development Corporation

BCArc was a sponsor organization for four grants from the United States Department of Housing and Urban Development to construct new residences for BCArc’s clients. Each grant required that a new single-purpose owner corporation be established. Four nonprofit corporations were established (on February 4, 2004; January 7, 2005; March 10, 2006; and January 18, 2007, respectively): Berkshire Community Apartments, Inc.; Hollow Road Development Corporation; Lanesboro Development Corporation; and Gamwell Development Corporation. These corporations are located at the same address as BCArc, and they all share some board members with Berkshire Omega; these members are all appointed by BCArc’s board of directors.

BCArc has contractual agreements with each sponsor corporation, under which each corporation agrees to pay BCArc a percentage of its gross rent collections in return for BCArc providing management services at the residences it operates.

3. Your Personal Best: Workshops for Success

The spouse of BCArc's president and CEO provides workforce development training, coaching, grant writing, program development, and department strategic planning services to BCArc through a contract with her company, Your Personal Best: Workshops for Success. During the audit period, BCArc paid her \$34,061 for professional services. In addition, BCArc's president and CEO was identified as an associate of her company on BCArc's website.

AUDIT OBJECTIVES, SCOPE, AND METHODOLOGY

In accordance with Section 12 of Chapter 11 of the Massachusetts General Laws, the Office of the State Auditor has conducted a performance audit of Berkshire County Arc, Inc. (BCArc) for the period July 1, 2017 through June 30, 2019.

We conducted this 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.

Below is a list of our audit objectives, indicating each question we intended our audit to answer; the conclusion we reached regarding each objective; and, if applicable, where each objective is discussed in the audit findings.

Objective	Conclusion
1. Are BCARC's management staff members qualified for their positions, and is their level of compensation reasonable and properly documented in accordance with its policies and procedures and Section 1.05(24) of Title 808 of the Code of Massachusetts Regulations (CMR)?	Yes
2. Are BCARC's credit card expenditures documented and allowable in accordance with its policies and procedures and 808 CMR 1.04(1), 1.04(5), 1.05(3), 1.05(9), 1.05(10), 1.05(12), 1.05(23), and 1.05(26)?	No; see Findings <u>1</u> and <u>4</u>
3. Does BCARC comply with all the requirements of 808 CMR 1.05(8) and 1.05(12) regarding related-party transactions?	No; see Findings <u>2</u> and <u>3</u>

To achieve our objectives, we gained an understanding of the internal controls we determined to be relevant to the objectives by reviewing all applicable Operational Services Division regulations as well as agency policies and procedures. We also conducted interviews with responsible agency officials about control activities. We evaluated the design and implementation of the relevant controls and tested their operating effectiveness over management employee compensation, credit card expenses, and related parties.

In addition, we conducted further audit testing, as described below.

Management Qualifications and Compensation

We tested whether all 45 management-level employees had qualifications that were consistent with their job titles and responsibilities. We did this by obtaining each management-level employee's resume, if available, and comparing the information therein to the employee's job title and job description, which listed job qualification requirements.

We obtained salary information for all management-level employees from BCARC's payroll records. We compared the annual salaries for these employees that were charged to BCARC's state contracts to the maximum salary amounts that can be charged to state contracts according to 808 CMR 1.05(24). We tested whether salary increases for these employees were reasonable. Specifically, we obtained the personnel files for all 45 management-level employees and reviewed the documentation in the files to determine whether the reasons for salary increases were documented and appeared to be reasonable, based on promotions and/or good performance evaluations. Further, we obtained a list of all 11 management-level employees who received executive compensation bonuses during the audit period. We reviewed all the documentation (Executive Compensation Bonus Reports) regarding the awarding of these bonuses to determine whether they were awarded consistently with the agency's policies.

Credit Card Expenses

During our audit period, BCARC had 51 credit cards. Three of these credit cards (2 for Best Buy and 1 for Sears) were not in use during our audit period; therefore, we only tested 48 credit cards, as follows.

We selected the entire populations of Citibank and American Express credit card purchases from our audit period. The Citibank population consisted of 2,855 purchases, totaling \$615,424; the American Express population consisted of 233 purchases, totaling \$18,881. We reviewed credit card statements and all available supporting documentation (e.g., receipts, invoices, and purchase orders) on file for these purchases to determine whether they were appropriate (i.e., related to BCARC's state-funded contracts), properly authorized, and documented.

We selected a nonstatistical, judgmental sample of 10 months of the 24-month audit period for the Home Depot, Walmart, and Staples credit cards. The Home Depot sample consisted of 280 purchases, totaling \$39,030; the Walmart sample consisted of 195 purchases, totaling \$31,916; and the Staples

sample consisted of 72 purchases, totaling \$8,739. We reviewed credit card statements and supporting documentation (e.g., receipts, invoices, and purchase orders) on file for these purchases to determine whether they were appropriate (i.e., related to BCARC's state-funded contracts), properly authorized, and documented.

We selected the entire population of Big Y credit card purchases from our audit period. This population consisted of 45 purchases, totaling \$3,348. We reviewed the receipts and supporting documentation (e.g., purchase orders) on file for these purchases to determine whether they were appropriate (i.e., related to BCARC's state-funded contracts), properly authorized, and documented.

We selected the entire population of ExxonMobil credit card gas purchases from our audit period. This population consisted of 1,011 purchases, totaling \$38,353. We calculated the average monthly expense, and using the number of vehicles BCARC owns, we calculated the average monthly expense per vehicle to determine whether the expenses seemed excessive.

During our review of BCARC's Citibank, American Express, and Home Depot credit card purchases, we found that in addition to using these cards to make business purchases, BCARC used them to purchase personal items and services for its clients. In those instances, we determined whether the Savings Withdrawal Forms required by BCARC's policies were on file and properly completed.

When nonstatistical sampling methods were used, we could not project the results of our testing to the population.

Credit Card Reward Travel Miles

Thirteen of BCARC's 48 credit cards were associated with credit card programs that allowed cardholders to accumulate reward travel miles based on the dollar value of purchases made on the card. We requested that BCARC officials provide us with a summary of the reward travel miles accumulated on these cards, as well as the miles used on them, during the audit period for both business and personal travel. In particular, we requested a summary of the reward travel miles used by BCARC's president and chief executive officer (CEO), because he was listed as the cardholder. The specific information we requested included the total number of reward travel miles used for business and personal purposes, flight destinations, and dates of travel. However, BCARC could only provide us with a summary of the total reward travel miles used during the audit period. Therefore, we interviewed BCARC's president and

CEO regarding this matter and reviewed agency cell phone bills to determine the dates and times when he appeared to have traveled. We interviewed 4 of the 11 members of BCARC's board of directors to determine whether they knew and approved of the president and CEO's use of reward travel miles earned from agency expenses.

Inventory

We obtained the inventory lists of non-generally accepted accounting principles⁵ equipment, furnishings, and other goods at BCARC's residential homes and administration buildings. We reviewed these lists to determine whether inventory was properly documented in accordance with 808 CMR 1.04, which requires unique asset identification (ID) numbers (tag or serial numbers), specific descriptions, purchase prices, and purchase dates. During our review of the Citibank, American Express, Home Depot, Walmart, and Staples credit card purchases, we found 316 inventory items purchased during the audit period, totaling \$73,711, which we compared to the inventory lists to determine whether the items were included.

Related-Party Transactions

We inspected BCARC's Uniform Financial Statements and Independent Auditor's Reports (UFRs) for fiscal years 2018 and 2019, including the notes related to Berkshire Omega, to determine whether BCARC properly disclosed its related-party transactions. We also inspected Berkshire Omega's audited financial statements, BCARC's Related Party Allocation Plan, Berkshire Omega's leases, Berkshire Omega's maintenance contracts, and Berkshire Omega's rent calculations to determine whether the disclosed related-party transactions were allowable in accordance with 808 CMR 1.05(8)(12).

We inspected the rent calculations for the properties owned by Berkshire Omega and leased to BCARC to determine how the rent payments were calculated and what they consisted of. Also, we inspected Berkshire Omega's audited financial statements and monthly financial statements to determine whether they contained any financial information related to BCARC.

5. The "Fixed Assets—Acquisition Policy" issued jointly by the Office of the Comptroller of the Commonwealth and the Operational Services Division defines such assets as follows: "**Singular** assets (including infrastructure) with the following characteristics: **vehicles, equipment, furniture, computer software, and all electrical and computer components** with (1) a useful life of more than one year and (2) with **an original cost between \$1,000 and \$49,999[;]** **Buildings and other infrastructure** with an **original cost between \$1,000 and \$99,999[;]** **Road infrastructure** with a **cost of less than \$99,999 per lane mile** for roads and bridges[;] **Software** costs **below \$50,000.**"

We requested the calculation/determination of the fair market rent costs for Berkshire Omega's properties during our audit period. We did not receive the calculation/determination because none has been performed since 2006.

We obtained and inspected BCARC's contracts with the spouse of BCARC's president and CEO, and her business Your Personal Best: Workshops for Success, and compared them to submitted invoices and service reports to determine whether the services provided were included in the contracts.

Also, we inspected BCARC's credit card transactions to determine whether the spouse of BCARC's president and CEO used and/or benefited from the credit cards.

Data Reliability Assessment

BCARC uses the Economized Time Services (ETS) Panorama system to record and process all accounting transactions. We determined the reliability of the data obtained from ETS by testing selected system controls (configuration management and contingency planning) that were in place during our audit period. Additionally, we performed validity and integrity tests, including (1) testing for blank fields, (2) scanning for duplicate records, and (3) looking for dates outside the audit period. We also selected a judgmental sample of 80 hardcopy supporting documents (e.g., credit card statements) and traced them to ETS data (e.g., general ledger account number, general ledger department number, and transaction amount) for agreement.

BCARC uses the Complete Payroll Solutions (CPS) system to manage and maintain employee attendance and other employee information, such as payroll, benefits, and applicant tracking. We determined the reliability of the data obtained from CPS by testing selected system controls (access controls, configuration management, contingency planning, and segregation of duties) that were in place during our audit period. Additionally, we performed validity and integrity tests, including (1) testing for blank fields, (2) scanning for duplicate records, and (3) looking for dates outside the audit period. We also performed the following tests:

- We selected a judgmental sample of 34 employees from CPS and traced them to hardcopy supporting documentation (e.g., employee personnel files that contained employee IDs, employee names, salary effective dates, and salary amounts) for agreement.
- We selected a judgmental sample of 21 employees from hardcopy supporting documentation (e.g., employee personnel files that contained employee IDs, employee names, salary effective dates, and salary amounts) and traced them to CPS data for agreement.

To assess the reliability of the total number of related-party organizations with which BCARC did business during the audit period, we reviewed BCARC's UFRs for fiscal years 2018 and 2019 and the Secretary of State's website.

We obtained a representation letter from BCARC management confirming that they had provided all credit card and related-party records.

Based on our audit work, we determined that the data obtained for our audit were sufficiently reliable for the purposes of our audit work.

DETAILED AUDIT FINDINGS WITH AUDITEE’S RESPONSE

1. Berkshire County Arc, Inc.’s use of its credit cards resulted in nonreimbursable expenses, unallowable use of reward travel miles, and improper administration of fixed assets.

During our audit period, we found issues with Berkshire County Arc, Inc.’s (BCArc’s) credit cards involving nonreimbursable expenses, credit card reward travel miles used for personal travel, and improper administration of fixed assets. These issues are described in detail below.

a. BCARC charged \$124,247 in nonreimbursable expenses to its state contracts.

During our audit period, BCARC used its credit cards to pay \$124,247 in expenses that were nonreimbursable under its state contracts because they were inadequately documented, were not related to BCARC’s social service program activities, or were types that were otherwise specifically prohibited by state regulations (e.g., luxury items). BCARC did not report these costs as nonreimbursable in the Uniform Financial Statements and Independent Auditor’s Reports (UFRs) it filed with the state Operational Services Division (OSD); this indicates that state contract funds were used to pay for them. BCARC could have used this \$124,247 to pay for reimbursable expenses for its state-funded programs.

A summary of the unallowable expenses by fiscal year follows.

Expenses	Fiscal Year 2018	Fiscal Year 2019	Total
Conference/Training Expenses without Adequate Documentation	\$ 10,689	\$ 19,383	\$ 30,072
Goods and Services without Adequate Documentation	15,795	17,865	33,660
Fundraising Expenses	7,417	10,226	17,643
Meals without Adequate Documentation	4,738	7,759	12,497
Non-Program General Expenses	6,089	5,925	12,014
Gifts and Gift Cards without Adequate Documentation	6,588	3,870	10,458
Non-Program Related-Party Expenses	5,689	1,375	7,064
Luxury Items	30	693	723
Late-Payment Fees and Penalties	51	65	116
Total	<u>\$ 57,086</u>	<u>\$ 67,161</u>	<u>\$124,247</u>

Luxury items included valet parking, priority boarding, main-cabin extra seating on airlines, and alcohol. Non-program general expenses included the production of BCARC customized, branded K-cups and a \$210 payment for a parking fee for an employee. Inadequately documented expenses included conference/training expenses; meals, goods, and services for which there was no documentation to substantiate the business purposes; and 578 gift cards for which there was no documentation of who the recipients were. Non-program related-party expenses were incurred by one of BCARC's related-party organizations but paid for by BCARC.

Authoritative Guidance

According to Section 1.04(1) of Title 808 of the Code of Massachusetts Regulations (CMR),

The Contractor . . . shall keep on file . . . supporting documents . . . which reflect . . . costs incurred in or allocated to any Program of services rendered under the Contract.

Section 1.05 of the regulation identifies the following unallowable costs:

- (3) Certain Interest.
 - (d) *Any interest or penalties incurred because of late payment of . . . indebtedness. . . .*
- (10) Fundraising Expense. *The cost of activities which have as their primary purpose the raising of capital or obtaining contributions, including the costs associated with financial campaigns, endowment drives, and solicitation of gifts and bequests. . . .*
- (12) Non-program Expenses. *Expenses of the Contractor which are not directly related to the social service Program purposes of the Contractor. . . .*
- (23) Luxury Items. *All costs associated with luxury items including . . . alcoholic beverages . . . and all non-Program entertainment expenses. . . .*
- (26) Undocumented Expenses. *Costs which are not adequately documented in the light of the American Institute of Certified Public Accountants statements on auditing standards for evidential matters.*

Additionally, the guidelines in OSD's *UFR Audit & Preparation Manual* require BCARC to identify any nonreimbursable costs it incurs in the UFRs it has to submit annually to OSD. According to this manual, if, during an audit, an auditor identifies any nonreimbursable costs that were not reported in an entity's UFRs, "it is presumed that Commonwealth and Federal funds have been used to defray non-reimbursable costs when those costs are not appropriately disclosed."

Reasons for Issue

BCArc's credit card policies and procedures are inadequate: they do not require staff members to submit sufficient documentation to support expenses, and they only require a purchase order and receipt, with no explanation of the business nature of expenses. In addition, BCArc's management has not established monitoring controls to ensure that required documentation is submitted and that any nonreimbursable expenses are identified before payment, reported as such on BCArc's UFRs, and not charged to state contracts.

Auditee's Response

The Office of the State Auditor (OSA) presumes that Berkshire County Arc, Inc. (BCArc) charged \$124,247 in nonreimbursable expenses to its State contracts because those expenses were not listed as "nonreimbursable" on BCArc's Uniform Financial Report (UFR). BCArc annually completes and files a UFR and Independent Auditor's Report with the State Operational Services Division (OSD) as required. BCArc employs independent auditors, [certified public accountants] specializing in audits of nonprofit entities. The UFR includes a breakdown of all reimbursable and nonreimbursable expenses.

OSA "presumed" that the non-reimbursable expenses were paid for with State funds because the expenses were not specifically listed as nonreimbursable on BCArc's UFR, not because there is any evidence that State funds were actually used to pay for the identified expenses. OSA's "UFR Audit and Preparation Manual" states that, "it is presumed that Commonwealth and Federal funds have been used to defray non-reimbursable costs when those costs are not appropriately disclosed" as nonreimbursable on the UFR. . . . Neither BCArc's independent auditors nor any of BCArc's regulatory and/or oversight agencies noted deficiencies in BCArc's use or reporting of State funds.

BCArc's funds are not segregated according to State vs. non-State sources, nor are expenses "charged" to certain contracts. Nevertheless, BCArc acknowledges that some of the funds identified as nonreimbursable by OSA were not correctly listed on its 2018 and 2019 UFRs. (As described below, a number of the expenses identified as nonreimbursable by OSA were in fact reimbursable.) However, State funds were not misused, nor were they used to pay for nonreimbursable expenses. BCArc had more than sufficient funds to pay the \$124,247 alleged by OSA to be nonreimbursable expenses. (\$124,247 amounts to <1% of BCArc's total revenue.) As illustrated in the table below, BCArc received nearly \$11 million (16% of its revenue), from non-State sources during the FY2018–2019 audit period—more than sufficient to pay for the \$124,247 in expenses considered nonreimbursable by OSA.

	<i>FY2018</i>	<i>FY2019</i>	<i>Total</i>
<i>Revenue from State sources:</i>	<i>29,738,683</i>	<i>31,295,825</i>	<i>61,034,508</i>
<i>Revenue from other sources:</i>	<i>5,935,295</i>	<i>5,876,620</i>	<i>11,811,915</i>
<i>Total BCARC Revenue:</i>	<i>35,673,978</i>	<i>37,172,445</i>	<i>72,846,423</i>

OSA concluded that there was "no documentation" identifying the recipients of 578 gift cards. OSA asked BCARC for specific files, which were promptly provided, but OSA never asked for an explanation of the gift cards or requested any documentation concerning the recipients of the gift cards. Had OSA asked, it would have been provided with a copy of the spreadsheet maintained by BCARC detailing each recipient. BCARC maintains the spreadsheet in its accounting files with a schedule of expenses. . . . The 578 gift cards—each for \$15—were provided to BCARC staff members as a reward for providing services that went "above and beyond."

OSA also concluded that certain expenditures, including valet parking, priority boarding and main-cabin extra seating on airlines, were luxury purchases. Here again, OSA apparently followed customary accounting guidance, but was not familiar with the population served by BCARC, and did not request an explanation for the expenditures. For example, had OSA asked, BCARC would have explained that extra main-cabin seating was purchased so an individual with disabilities could attend the National Self Advocacy Conference in 2018.

Although it is a leader in providing service to individuals with intellectual and developmental disabilities, BCARC recognizes that there are always improvements to be made to its bookkeeping systems and its financial policies and procedures. BCARC acts on guidance from OSA, as well as its independent auditors, to ensure compliance with State contracts and proper internal controls.

In response to OSA’s draft audit report BCARC’s Board of Directors (BBOD) updated and revised its credit card policies and procedures in March 2020. . . . The new policies require additional information and documentation for all business expenses. BCARC also updated its old external training form. . . . BCARC adopted a new External Training Form and protocol that requires additional information and recordkeeping. . . . BCARC staff are recognized for their advocacy and participation in regional as well as national training and educational seminars. BCARC’s new procedures will ensure that all such participation is properly documented.

Auditor’s Reply

As noted above, according to OSD guidelines, if, during an audit, an auditor identifies any nonreimbursable costs that were not reported in an entity’s UFRs, “it is presumed that Commonwealth and Federal funds have been used to defray non-reimbursable costs when those costs are not appropriately disclosed.” It is typical, and often most practical, for organizations like

BCArc to commingle their state and non-state funds except those that may have restrictions on their use, such as certain donations. This is why OSD requires human service providers such as BCArc that contract with state agencies to be transparent about their nonreimbursable expenses, requiring providers to identify and report them, along with the source/s of non-state funds used to pay for them, in UFRs. OSD's guidance regarding the audit of nonreimbursable expenses must be followed by any auditors, public and private, who conduct audits of contracted human service providers, and it was the guidance the Office of the State Auditor (OSA) appropriately followed in this audit.

We cannot comment on the results of audits conducted at BCArc by other auditors. However, as noted above, our audit found \$124,247 in expenses that we determined were nonreimbursable under BCArc's state contracts because they were inadequately documented, were not related to BCArc's social service program activities, or were otherwise specifically prohibited by state regulations. Although BCArc may have had sufficient non-state funds to pay for these expenses according to its UFRs, the funds were not used to do so.

During our audit, OSA asked BCArc to provide us with all the credit card statements, and supporting documentation for the expenses indicated on the statements (including the gift cards), for the audit period. BCArc did not provide us with any information about these gift cards during our audit fieldwork, but with its response, it provided a gift card spreadsheet that purported to detail who received the gift cards, in what years they received them, and how much they received. However, this documentation was incomplete; the dollar value of gift cards distributed according to the spreadsheet does not equal the dollar value of the gift cards OSA identified and questioned. In addition, some of this information appears to be inaccurate. In its response, BCArc asserted that each of the 578 gift cards had a value of \$15. However, based on the documentation OSA reviewed, they had values of \$10 to \$100.

Contrary to what BCArc states in its response, OSA is familiar with the population BCArc serves. The reason OSA is questioning the main-cabin extra seating expense is that the supporting documentation that BCArc provided to OSA indicated that it was purchased by and for BCArc's chief operating officer (COO), with no indication that it would be used by one of BCArc's clients.

Based on its response, BCArc is taking measures to address this problem, but we urge it to fully implement all our recommendations on this issue.

b. BCArc's president and chief executive officer used agency credit card reward travel miles for his personal travel.

BCArc's president and chief executive officer (CEO) redeemed credit card reward travel miles earned by BCArc on agency credit cards for his personal use. The president and CEO opened credit card accounts with two different card companies—American Express and Citi—identifying both himself and BCArc as cardholders. Additional cards, which were linked to his account, were issued to various BCArc employees and used to pay for agency expenses. Consequently, all miles earned on these cards accrued to the account in the president and CEO's name; most of the miles, however, were earned by BCArc charging expenses to the cards.

During our audit period, more than 930,000 miles were earned on the CitiBusiness/AAdvantage Platinum Select card. Of these miles, 625,358 (approximately 67%) were earned from BCArc-related expenses; the others were earned from personal purchases made by the president and CEO that were not paid for by BCArc. According to the president and CEO, he redeemed more than 400,000 of the 930,000 miles. Although BCArc did not provide us with information about his use of the miles, we determined through our analysis that at a minimum, the president and CEO redeemed miles earned by BCArc on agency credit cards to pay for trips made for personal reasons to Hawaii and Mexico.

As a result of this issue, BCArc lost the opportunity to reduce its travel costs (e.g., the miles could have been used for BCArc employees traveling to conferences); the money saved could have been used to provide additional services to its clients.

Authoritative Guidance

BCArc has a Corporate Compliance Program, of which the president and CEO has been designated the Corporate Compliance Officer. The program's *Guiding Principles* document states,

[The] Corporate Compliance Program is intended to promote adherence to the highest standards of business and ethical conduct in all aspects of agency operations and to ensure conformance to all federal, state, and local statutory and regulatory obligations. . . .

- *No agency staff person or board member will engage in any transaction involving the agency in which they have a financial or personal interest.*

This would include the use of agency credit cards for personal benefit.

Under OSD regulation 808 CMR 1.05(9)(a), fringe benefits are nonreimbursable under state contracts "to the extent that they are not available to all employees under an established policy of the Contractor." BCARC does not have an established fringe benefit policy that allows its staff to make personal use of miles BCARC has earned.

Reasons for Issue

BCARC's policies and procedures did not require all cards to be issued in the agency's name rather than those of individual employees. In addition, there is no documentation that the board of directors knew of or consented to the president and CEO's use of these miles. During our interviews with 4 of the agency's 11 board members, only 1 member stated that he knew the president and CEO had used these miles. The other 3 stated that they did not know. None of the board minutes indicated that the full board was aware of this situation.

Auditee's Response

BCARC's CEO was required to guarantee the credit cards used by BCARC, making the CEO personally liable for the payments. . . . This was a normal requirement, and to the best of BCARC's knowledge, remains so for most nonprofits in Massachusetts or the United States. As a result, the airline mileage points at issue in the Audit Report were credited to the CEO, as credit card and airline miles accounts were limited to or benefited only an individual and not an organization at the time of their inception.

During the Audit Period, the CEO utilized 475,000 of the airline miles, representing 170,213 more airline miles than the CEO's personal card contributed to the account. . . .

The CEO has offered to make a voluntary contribution, in lieu of the miles, to the Agency for all of the remaining airline mileage points (both BCARC- and CEO-earned) in the account, even though they are of little value to BCARC, especially during the pandemic, and are expiring in 2022. These funds as directed by the BBOD will be placed into the "Fundraising Account," which is solely used to provide for individuals who do not have the financial ability to pay for incidental personal needs.

In further response to the inquiry from OSA about the airline miles, the BBOD and CEO implemented a complete review of BCARC credit card policies and procedures and updated and approved new policies and procedures regarding BCARC's credit cards, and to end the use of airline miles tied to BCARC's credit card use. BCARC also applied for and secured a new credit card without personal recourse (i.e., not secured by an individual, although BCARC is required to submit personal info and [supplemental security income] per the Patriot Act). BCARC will continue to pursue a replacement for the CEO-secured

credit card, provided it offers an adequate limit, to completely separate any CEO from liability.

The BBOD revised its CREDIT CARD POLICIES AND PROCEDURES as follows:

- 1. BCARC policy prohibits personal use of credit card benefits (points, cash backs, airline miles, etc.) by any individual.*
- 2. Any and all credit card benefits inure to the benefit of BCARC.*
- 3. Existing points will solely benefit BCARC.*
- 4. Any credit card benefits previously used by the CEO, who personally secured the cards, have been fully ratified and confirmed by the Board as an additional de minimis [too minor to merit consideration] fringe benefit for the CEO under his existing employment agreement.*

Auditor's Reply

Whether or not the president and CEO was required to guarantee the credit cards used by BCARC, we believe he should have accounted for the reward travel miles earned through purchases made by BCARC and ensured that they were used for business, not personal, travel. As noted above, personal use of reward travel miles earned by BCARC is inconsistent with agency policy and is, in OSA's opinion, noncompliant with OSD regulations. BCARC's board seems to agree with our concerns, as it has already taken action to stop this activity.

Also, BCARC does not dispute that its CEO used reward travel miles for personal travel. As noted in our report, OSA asked BCARC staff to provide a full accounting of the reward travel miles used by the president and CEO for business and personal purposes so that we could perform a full analysis of this issue. BCARC personnel stated that they could not provide this information. The CEO did provide OSA with a written summary of his reward mile use during the audit period, however. This information could not be verified, so we used other documentation to obtain an understanding of where he traveled during the audit period.

Based on its response, BCARC has taken measures to stop this practice. We recommend that it fully implement all our recommendations on this issue.

c. BCarc did not properly administer its inventory of non–generally accepted accounting principles fixed assets.

During our audit period, BCarc did not properly administer its inventory of non–generally accepted accounting principles (GAAP) fixed assets. Specifically, its inventory records lacked key information on each asset, including unique asset identification numbers (tag or serial numbers), specific descriptions, purchase prices, and purchase dates. Therefore, BCarc cannot perform a periodic physical inventory of these assets; this makes them highly susceptible to theft or misuse. In fact, 109 assets (which included air conditioners, a television, a camera, an electric snowblower, and a printer), costing \$23,401, that BCarc purchased during our audit period could not be found on its inventory list.

Authoritative Guidance

Regarding inventory of equipment, furnishings, and other non-GAAP fixed assets, the “Fixed Assets—Acquisition Policy” issued jointly by the Office of the Comptroller of the Commonwealth and OSD states,

Non–GAAP Fixed Assets must be recorded in a Department’s inventory and reconciled at least annually. This inventory can be either electronic or on paper, as long as it records the date of purchase, amount, description, location and disposition of an item.

Although not required, this represents best practices that BCarc should follow.

Reasons for Issue

BCarc does not have any policies and procedures for administration of its inventory of non-GAAP fixed assets.

Auditee’s Response

BCarc maintains inventory of all capital items valued at \$5,000 or more in accordance with the Agency Capitalization Level that BCarc uses pursuant to its contracts. The inventory of all capitalized items is maintained and kept properly in accordance with Generally Accepted Accounting Principles (GAAP). OSA included a list of 109 items that it maintains should be inventoried. These items were not inventoried because they are valued from \$9.99 to \$2,078.63, well below BCarc’s capitalization level. . . . OSA’s list also included disposable items that would not be included in an inventory of Capital Items, such as soil test kits, folders, and 3-ring binders. OSA did not ask about BCarc’s contractual capitalization levels. BCarc’s capitalization change . . . demonstrates that BCarc’s capitalization level begins at \$5,000 for items not purchased with State funds;

BCArc also maintains inventory of any and all assets bought by the State, regardless of value, under "State-owned assets." The items called out by OSA are not State-owned assets.

Auditor's Reply

Although BCArc maintained an inventory of its GAAP⁶ fixed assets, it did not properly administer its inventory of non-GAAP fixed assets. OSA acknowledges that BCArc is not required to maintain an inventory of its non-GAAP fixed assets; however, we believe this is a best practice it should follow. Maintaining an inventory of non-GAAP fixed assets is required of all state agencies and safeguards many inventory items, such as cameras, televisions, and printers, that are highly susceptible to theft. Also, BCArc did not provide documentation to indicate that it had developed policies and procedures for the administration of its inventory of fixed assets, a fact that BCArc does not dispute in its response.

In its response, BCArc identifies non-GAAP inventory items, such as disposable items, that it believes are not of significant value. However, OSA's testing in this area involved sampling anything characterized by BCArc's accounting records as equipment and furnishings, regardless of its nature or value. Also, the soil test kit was not counted as a separate inventory item but was included with a greenhouse, which could not be located on the inventory list.

Recommendations

1. BCArc should cooperate with OSD and determine how much of this \$124,247 of nonreimbursable credit card expenses BCArc should reimburse to the Commonwealth.
2. BCArc should amend its policies and procedures to ensure that all credit card expenses are properly documented according to OSD regulations.
3. BCArc management should establish monitoring controls to ensure that management reviews all credit card expenses before payment and determines whether they are reimbursable to BCArc's state contracts.
4. BCArc should properly identify and correctly report all nonreimbursable expenses on its UFRs.

6. The "Fixed Assets—Acquisition Policy" issued jointly by the Office of the Comptroller of the Commonwealth and OSD defines such assets as follows: "**Singular** assets (including infrastructure) with the following characteristics: **All land**, regardless of cost[;] **All works of art and historical treasures**, regardless of cost, acquired or donated to a department after July 1, 2001[;] **Vehicles, equipment, furniture, computer software, and all electrical and computer components** with a useful life in excess of one year and with an historical cost **in excess of \$49,999**[;] **Buildings purchased or constructed** . . . with an historical cost of **greater than \$99,999**[;] **All road infrastructures** with an historical cost **in excess of \$99,999** per lane mile for road assets[;] **All computer software**, whether internally or externally developed[;] Software costs above \$50,000, but below \$1,000,000, are considered a GAAP fixed asset."

5. BCARC should stop using the American Express and Citibank cards that are linked to the president and CEO’s account and obtain new cards issued in its own name.
6. BCARC should enhance its policies and procedures to require that all cards be issued in its name and that any travel rewards or other incentives issued by card companies be used solely for its benefit.
7. BCARC’s board should provide effective oversight over cards by periodically reviewing card statements to determine whether rewards are earned and how they are used.
8. BCARC should develop policies and procedures for the administration of its non-GAAP fixed assets that include a requirement that its inventory records contain all key information and be maintained and current for each asset as suggested in the “Fixed Assets—Acquisition Policy.”

2. BCARC charged at least \$651,540 in unallowable related-party expenses against its state contracts.

During our audit period, BCARC charged at least \$651,540 in unallowable related-party expenses against its state contracts. These costs were for capital improvements, maintenance, and bookkeeping. BCARC paid for the capital improvements for properties owned by Berkshire Omega. Although Berkshire Omega has listed the cost of these capital improvements in its financial statements as an account payable to BCARC, there are no formal loan agreements or repayment schedules that establish when, if ever, Berkshire Omega must repay it. These expenses are non-program-related, because they benefited Berkshire Omega, and therefore should not have been charged to BCARC’s state contracts. BCARC could have used this \$651,540 to pay for reimbursable expenses for its state-funded programs.

BCARC performs the maintenance at Berkshire Omega’s properties even though its lease agreements with Berkshire Omega require Berkshire Omega to provide it. BCARC also performs Berkshire Omega’s bookkeeping. The following table summarizes the expenses for which BCARC paid during our audit period.

Services Provided to Berkshire Omega by BCARC

Expense	Fiscal Year 2018	Fiscal Year 2019	Total
Bookkeeping	\$ 4,621	\$ 5,372	\$ 9,993
Property Maintenance	51,402	102,804	154,206
Total	<u>\$ 56,023</u>	<u>\$ 108,176</u>	<u>\$ 164,199</u>

BCARC invoices Berkshire Omega for this maintenance and bookkeeping; however, each year, BCARC calculates what rent it will pay for each of the properties it rents from Berkshire Omega based on

Berkshire Omega's operating costs. These costs include payments to BCARC for its bookkeeping and maintenance. Consequently, BCARC ultimately pays for these expenses via the rent payments it makes to Berkshire Omega. In addition, since the expenses are related to the operation of Berkshire Omega and therefore are non-program expenses, BCARC should not have charged them to its state contracts.

Finally, according to OSD regulations, BCARC is only allowed to pay Berkshire Omega rent in an amount equal to either the fair market rent for the properties or Berkshire Omega's actual costs for operating them, whichever is less. However, BCARC has not conducted a fair market rent determination for these properties since 2006. Therefore, BCARC cannot be certain that its rent payments to Berkshire Omega are consistent with OSD regulations.

Authoritative Guidance

Under 808 CMR 1.05(12), "expenses of the Contractor which are not directly related to the social service Program purposes of the Contractor" are nonreimbursable under state contracts. Since these expenses were not budgeted for in BCARC's state contracts, they are non-program-related expenses.

In addition, 808 CMR 1.05(8) identifies which related-party transaction costs (such as rent) are reimbursable:

Costs which are associated with a Related Party transaction are reimbursable only to the extent that the costs do not exceed the lower of either the market price or the Related Party's actual costs.

Reasons for Issue

BCARC management stated that although a fair market rent determination had not been performed since 2006, they believed they were paying below fair market rent for properties that BCARC rented from Berkshire Omega. They also stated that since BCARC controlled Berkshire Omega, capital improvements were to be repaid the following year.

BCARC management also stated that maintenance and bookkeeping were ultimately provided by Berkshire Omega through separate contracts with BCARC. However, as noted above, the maintenance expenses were to be provided by Berkshire Omega in accordance with its lease agreements, and BCARC should not be paying for any of Berkshire Omega's expenses, since they are unallowable under OSD regulations.

Recommendations

1. BCARC should cooperate with OSD to resolve any identified issues regarding nonreimbursable costs and should reimburse the Commonwealth for any such costs that OSD determines must be repaid.
2. BCARC should perform a fair market rent determination for the properties it leases from Berkshire Omega annually and use this information to determine what rents it should pay Berkshire Omega for these properties (i.e., the lower of the fair market rent or Berkshire Omega's actual costs related to the properties).
3. BCARC should stop using state funds to pay for any capital improvements to Berkshire Omega's properties and should enter into repayment agreements with Berkshire Omega for the capital improvements for which it has already paid.
4. BCARC should not pay for the maintenance of Berkshire Omega's properties or its bookkeeping expenses.

Auditee's Response

Berkshire Omega Corporation (BO) is a non-profit entity established by BCARC to hold title to real estate occupied by BCARC. BO's properties are 100% occupied and utilized by BCARC for residential services, day services, programming, and operations. BO was established by BCARC based on legal advice by BCARC's counsel and with full disclosure and knowledge of the Commonwealth of Massachusetts. The relationship is well-documented and disclosed in both organizations' financial statements as corroborated by BCARC's independent external auditors. . . .

The main purpose of this legal structure is to keep the real estate operations (BO) separate from the organization providing services (BCARC). The structure in place meets then and current State regulations and neither organization, nor any individual, is improperly benefiting from the relationship.

As OSA recognizes, Massachusetts regulations regarding related parties govern the amount of BCARC's lease payments to BO. 808 Mass. Reg. 1.05(8), states:

*(8) Related Party Transaction Costs. Costs which are associated with a Related Party transaction are reimbursable only to the extent that the costs do not exceed the lower of either the market price or **the Related Party's actual costs**. (Emphasis added.)*

BO leases the real estate to BCARC at cost. . . . It does not make a profit. BO's costs include bookkeeping, maintenance and capital improvements. The amount of the rent is determined annually by BCARC's external auditors and is based on the previous year's expenses. In accordance with Massachusetts regulation 1.05(8), BCARC's lease payments are based on BO's actual costs—including bookkeeping, maintenance and capital improvements. . . .

It is difficult to reconcile OSA's statement that "BCARC should not be paying for any of Berkshire Omega's expenses" when Massachusetts regulations require that BCARC pay "the lower of either the market price or the Related Party's actual costs." If it is preferred that BCARC make a single

lease payment based on BO's actual costs, rather than reimbursing BO for its actual costs, BCARC is willing to do so.

Because BO is a nonprofit organization that leases its real estate to BCARC at cost, BCARC and BO are confident that BCARC's lease payments are below the fair market rental rate. Nevertheless, because BCARC has not recently obtained a fair market rent determination for the leased properties, BCARC will obtain such a determination and will update its leases to reflect any necessary rental changes.

As a nonprofit entity operating at cost, BO has no retained surplus and therefore does not have funds to make capital purchases. BCARC therefore lends funds to BO for capital projects. All funds advanced to BO are drawn from BCARC's "Retained Surplus" accounts. State funds were not used to advance monies to BO. A majority of the funds advanced during the audit period were used by BO to purchase land for new housing at the request of the State. There are no current outstanding receivable balances owed to BCARC by BO. . . . In the future BCARC will document advances to BO as no-interest loans.

Finally, neither BCARC nor BO are aware of any issues that would have made payments between the two non-profit entities nonreimbursable as asserted by OSA. BCARC's auditors' report states:

*Although BCARC's primary funding is from state contracts, it does have other significant sources of revenue. While **we don't anticipate that ultimately there will be any expenses deemed to be non-reimbursable** as a result of this audit, **any expenses that might be deemed so would have been funded by those other sources, would not have been charged to state contracts, and therefore would not result in a reimbursement to the Commonwealth.** . . . (Emphasis added.)*

Auditor's Reply

OSA acknowledges the relationship between BCARC and Berkshire Omega and has provided a detailed description of this relationship in this report. OSA does not take issue with this relationship but rather with BCARC's payments to Berkshire Omega. Our report correctly points out that BCARC should only pay Berkshire Omega for expenses that are allowable under OSD regulations. As noted above, we found several expenses that BCARC paid during our audit period that were not allowable under OSD regulations. Specifically, BCARC paid for \$487,341 in capital improvements to properties owned by Berkshire Omega. These expenses are for assets that are not owned by BCARC and are non-program-related. In its response, BCARC states that because Berkshire Omega is a nonprofit entity like BCARC, it does not have sufficient funds to make these capital purchases. However, with its response, BCARC provided documentation that indicates that Berkshire Omega does not owe it any money related to these capital improvements. Thus Berkshire Omega apparently was able to obtain funding from some source to pay for them. Of particular concern is that although Berkshire Omega listed the cost of the

capital improvements in its financial statements as an account payable to BCARC, there was no formal loan agreement or repayment schedule that established when, if ever, Berkshire Omega must repay it.

In its response, BCARC states "All funds advanced to [Berkshire Omega] are drawn from BCARC's 'Retained Surplus' accounts. State funds were not used to advance monies to [Berkshire Omega]." However, this is not accurate, because the source of the funds in BCARC's Retained Surplus account is state contract funding, which is subject to OSD regulations. Surplus funds cannot be used to pay for any expenses that are unallowable under OSD regulations, such as the related-party transactions discussed above.

Regarding the maintenance expenses, as noted above, BCARC's leases with Berkshire Omega for the properties in question include a provision for Berkshire Omega to pay for property maintenance. Therefore, it is unclear why BCARC would provide these services if Berkshire Omega believed it could provide or pay for them as stated in the leases. Further, BCARC gave us documentation that indicated that the costs of bookkeeping and maintenance were included in Berkshire Omega's rent calculations for the properties it leased to BCARC. Thus BCARC pays for these expenses twice: once by paying directly and again in its rent. Moreover, although OSD regulations allow organizations to pay for certain related-party expenses, state contract funds are not to be used to perform services related to the operation of the related party, such as bookkeeping and maintenance.

Finally, although we acknowledge that BCARC had other non-state funding sources, it did not indicate in its UFRs that any non-state contract funding was used to pay for any of the expenses discussed in this finding. Based on its response, BCARC is taking some measures to address our concerns in this area. We urge it to fully implement our recommendations.

3. BCARC allowed inappropriate use of its credit cards.

During our audit period, a contracted employee who was a BCARC related party—the spouse of BCARC's president and CEO—either used or benefited from 14 BCARC credit card purchases, totaling \$2,057. For 7 of these purchases, she used BCARC's American Express card—the one assigned to BCARC's president and CEO—to purchase gifts for a BCARC-related conference. The remaining 7 purchases were for her to participate in BCARC-related activities with her spouse and included dinners, meetings, and hotel stays, of which only two purchases, totaling \$392, were reimbursed to BCARC. Personal use of a company credit card is an unsound business practice and creates a higher risk of card misuse.

Authoritative Guidance

BCArc's contract with the person in question states, "I understand that as a non-employee I am not eligible for any of the BCARC employee benefits." This would include the use of any company credit cards. The contract also states, "The Facilitator is not an employee of Berkshire County Arc. The Facilitator understands and agrees that Berkshire County Arc will not provide to the Facilitator any benefits or services."

Reasons for Issue

BCArc's president and CEO stated that these purchases were for legitimate agency expenses. BCARC credit card policies do not expressly restrict the use of cards to employees, and there are no monitoring controls in place to detect any card use by any unauthorized individuals, such as contractors.

Recommendations

1. BCARC should amend its credit card policies to limit card use to employees and establish monitoring controls to ensure that all employees and contractors comply with this requirement.
2. BCARC should improve its internal controls over credit cards to prevent the cards from providing a personal benefit to anyone.

Auditee's Response

BCARC adheres to a formal conflict of interest policy and at no time did the wife of BCARC's CEO (Consultant) use a BCARC credit card.

The Consultant was contracted to help organize and run a family support conference for the Berkshires, an assignment that was fully divulged and approved by BBOD vote prior to BCARC entering a contract with Consultant for services. The Consultant was hired and supervised by the COO—not the CEO—who reviewed . . . the program, budget, and progress with the BBOD. The Consultant discounted her rate and charged below-market value for her fee. The Consultant is uniquely qualified to deliver the contracted programs to BCARC employees.

In preparation for this conference at issue, the Consultant and the organizing committee sought approval to purchase numerous items for the conference, which were approved by the COO . . . who arranged for the purchase of the items. At no time did the Consultant use a BCARC credit card to make these purchases—they were made by BCARC staff.

Auditor's Reply

The documentation provided to us by BCARC, both during our audit and with its response, indicates that the purchases in question were made by the consultant and were not approved by the COO until after

they were made. Further, BCARC does not comment on the seven purchases we found that the consultant made to pay for her personal expenses associated with participating in BCARC-related activities with her spouse, only two of which (totaling \$392) were reimbursed to BCARC.

We again urge BCARC to implement all our recommendations on this matter to prevent these issues from reoccurring.

4. BCARC did not have required documentation for \$43,192 in client fund expenditures.

During the audit period, BCARC charged its Client Funds⁷ account \$43,192 in credit card purchases for which it did not have the required documentation (a completed Savings Withdrawal Form signed by the client, indicating that the client had approved the expenditure). These purchases included an air conditioner, a television, iPads, a computer, concert tickets, amusement park tickets, cruise tickets, hotel stays, and flights. As a result of this issue, there is inadequate assurance that all expenses charged to this account were incurred with client knowledge and consent.

Authoritative Guidance

BCARC's policies and procedures require the use of a Savings Withdrawal Form in withdrawing or transferring a client's funds. This form includes signature lines for the client, site manager, director of residential services, and president and CEO (or designee). The "Individual Funds Procedure" states,

All withdrawals or transfers of individuals' funds will require the approval of the appropriate Director and the President & CEO or designee on the Savings Withdrawal Form.

Reasons for Issue

BCARC did not have monitoring controls in place to ensure that its staff completed Savings Withdrawal Forms when using client funds to pay for expenses.

Recommendation

BCARC should develop procedures to monitor the use of client funds to ensure that all expenses paid for with these funds are properly approved using the Savings Withdrawal Form.

7. Some clients in BCARC programs receive personal funds from sources, such as Social Security disability insurance from the Social Security Administration and funds from family members and others, that are maintained in client fund accounts.

Auditee's Response

BCArc follows Social Security Administration [SSA] regulations for administering individuals' funds and undergoes successful annual independent audits without findings. According to SSA regulations, a Representative Payee is appointed when a person is deemed incapable of managing their monies. BCARC is the designated Representative Payee for a large majority of the individuals it serves. Many of the individuals served by BCARC are not able to approve and sign off on the expenditure of their own funds.

Previously, BCARC left the signature line blank if the individual was incapable of signing his/her name. BCARC employees have been instructed to write "non-applicable" if the individual is unable to sign his/her name and BCARC is the Representative Payee. All expenditures for clients had approved Savings Withdrawal forms that were provided to OSA. BCARC maintains strict policies concerning the use of Individual Funds. . . . In addition, BCARC updated the Savings Withdrawal . . . form to read "if applicable" under the individual's signature line. Additionally, a new Savings Withdrawal form has been implemented . . . when individuals are unable to sign for themselves. OSA has been provided all of the documentation.

BCARC states unequivocally that all client fund expenses were legitimate. In addition, BCARC's credit card policies and procedures, updated in March 2020, provide sufficient control over funds. When a purchase is made with an individual's funds, it is listed on the Weekly Individual Spending Form, which is reconciled with receipts that are submitted weekly to the Finance department pursuant to the procedures. . . . Those receipts and related documentation are stored within an individual's file (not within the credit card files).

Most of the reimbursement documentation requested by the State Auditor was not filed with the actual credit card invoices, but instead within the file of the individual who benefited from the expenditure, as is the practice of BCARC (to provide accurate accounting of the services needed by each individual); therefore, what appeared to be a lack of backup documentation was merely a difference in where the backup was filed. OSA never requested the supporting documents and apparently assumed that since they were not in the credit card files, they didn't exist. OSA has now been provided all of the backup documentation.

Auditor's Reply

In its response, BCARC states, "BCARC follows Social Security Administration regulations for administering individuals' funds." To do this, BCARC would have needed to establish and follow effective policies and procedures for the administration of these funds. This did not always happen.

Specifically, as noted above, BCARC's policies and procedures require the use of a Savings Withdrawal Form in withdrawing or transferring a client's funds. This form includes a signature line for the client, indicating that the signature is required. BCARC's policies and procedures do not address the process its staff must follow if a client cannot sign this form. During the audit, OSA requested all documentation related to the expenditures in question. We reviewed the documentation and found instances where

BCArc personnel wrote "unable to sign" on the signature line. Although there was no BCArc policy that clearly allowed this annotation instead of a client signature, we are aware that some of BCArc's clients may not be able to sign this document, and we accepted all the forms that had this annotation as acceptable documentation. The expenditures we questioned were ones that were not signed by clients, where the signature line had a note saying "unavailable for signature." OSA understood this notation to mean that the client was able to sign the form but BCArc personnel did not exercise due diligence in making sure that the purchase was made with the client's knowledge and consent.

In addition, some of the documentation BCArc provided appeared to be questionable. Specifically, one of the Savings Withdrawal Forms BCArc provided to us indicated that the form was "Reviewed & Revised 1/2021," but it was for a client expenditure in 2019, and the approval signature on the form was from 2019.

Our testing in this area was not intended to specifically identify improper use of client funds but rather to determine whether BCArc had implemented effective internal controls over the administration of these funds that ensured that expenditures of the funds were proper. Based on the issues we identified in this area, we urge BCArc to implement our recommendation.

APPENDIX

Berkshire County Arc, Inc. Program Descriptions⁸

Residential Services

Berkshire County Arc currently supports more than 165 individuals in community homes, cooperative and staffed apartments, supported living and home ownership throughout Berkshire and Hampden Counties. The Residential Services Program serves individuals in Brain Injury Services and Developmental Disability Services.

Day Habilitation

Services at our Day Habilitation Centers are person-centered and designed to meet the specific needs of each person we support. Day Habilitation Service Plans are developed in consultation with qualified and licensed therapeutic staff (including Physical Therapists, an Occupational Therapist, and Speech and Language Pathologists.) Each person also receives nursing support, including health status monitoring and coordination with other health care professionals.

Our outstanding and dedicated support staff work to provide individualized skills training in the following developmental areas:

- *Self-help*
- *Communication*
- *Sensory motor and mobility*
- *Independent living*
- *Social development*
- *Affective development*
- *Behavior development*

Adult Family Care

The program currently serves more than 125 qualified individuals in their own homes, or the homes of their caregivers. . . .

Our Services:

- i. Developing assessments to determine eligibility and level of care*
- ii. Providing a non-taxable monthly stipend to caregivers*
- iii. Providing nursing oversight*

8. Quotations in this appendix are from the Berkshire County Arc, Inc. website.

- iv. Providing case management and support services*
- v. Facilitating connections with other community organizations and service providers*
- vi. Assisting with future planning*
- vii. Providing family support and advocacy*

Advocacy and Family Support

Berkshire County Arc's Advocacy and Family Support services are designed to support children and adults with disabilities living in the community with their families.

The services include self-advocacy groups, a family support center, and respite services.

Down Syndrome Family Group

The Berkshire County Arc Down Syndrome Family Group is comprised of over 40 families throughout Berkshire County, working to advocate for and educate the public about Down syndrome and people with disabilities.

Zip 'N Sort Mail Services

Zip 'N Sort Mail Services, the largest mail service business in the Berkshires, maintains an integrated work setting for employees, with and without disabilities. Employees use state-of-the-art, automated equipment to satisfy its customer base of nearly 400 local, national and international companies.

Employment Services

Berkshire County Arc Employment Services provides comprehensive, individualized employment services that help people with a wide range of disabilities succeed in life and work.

Community-Based Day Services

BCArc offers two separate programs that focus on integrating individuals with the community to achieve a range of goals.

The Transitions program allows individuals to learn independence and gain employment skills. The Northview program is a community-based program that helps individuals “maintain personal, social, and community growth.”

Pooled Trusts

Berkshire County Arc's Master Special Needs Pooled Trust and Family Special Needs Pooled Trust . . . [protect] the assets of individuals with disabilities and still [maintain] eligibility for public benefits including MassHealth and [Social Security Disability Insurance].

Master Special Needs Pooled Trust is funded with assets of the individual, i.e., retroactive disability award, personal injury settlement, divorce, sale of a house. . . .

Family Special Needs Pooled Trust is funded with assets of a third party such as a parent or grandparent of a disabled person, rather than with the assets originally owned by the person with a disability (i.e., will, insurance policy, or savings).