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INDEPENDENT STATE AUDITOR'S REPORT ON CERTAIN ACTIVITIES OF ROAD TO RESPONSIBILITY, INC.

JULY 1, 2004 TO DECEMBER 31, 2007

OFFICIAL AUDIT REPORT

JANUARY 30, 2009

TABLE OF CONTENTS/EXECUTIVE SUMMARY

Road to Responsibility, Inc., (RTR) was incorporated in November 1988 as a private, nonprofit corporation to provide residential, social, vocational, recreational, counseling, and educational services to more than 1,000 consumers with mental and other disabilities who reside in Southeastern Massachusetts. These services include employment and training (day workshops), residential, day habilitation and Venture Program (community outreach) work and recreation programs. During the period covered by our audit, RTR employed approximately 400 staff and maintained its headquarters at Library Plaza in Marshfield.

During fiscal year 2008, the Office of the State Auditor (OSA) received information that raised concerns about certain activities of RTR and its administrative staff. As a result of these concerns, and in consultation with RTR's principal state purchasing agency, the Department of Mental Retardation (DMR), the OSA initiated an audit of RTR. The scope of our audit was to examine various administrative and operational activities of RTR during the period July 1, 2004 to December 31, 2007. We conducted this performance audit in accordance with Generally Accepted Government Auditing Standards. Our audit objectives consisted of a determination of whether RTR had implemented effective internal controls and an assessment of RTR's business practices and its compliance with applicable laws, rules, and regulations, as well as the various fiscal and programmatic requirements of its state contracts.

Our audit identified several issues. Specifically, we found that during our audit period (1) RTR provided as much as $621,847 in unnecessary compensation to certain members of its administrative staff, contrary to state regulations and without the knowledge and consent of RTR's Board of Directors; (2) RTR's President non-competitively awarded a $1.6 million construction contract; (3) RTR incurred $26,299 in unallowable bonus and fringe benefit expenses; (4) RTR did not always comply to the terms and conditions of its state contracts and its own personnel policies and procedures relative to time and attendance records, performance evaluations, and the maintenance of personnel files; (5) RTR did not efficiently operate two of its residential programs and consequently had to obtain an additional $80,749 in Commonwealth funding above the original contract amounts to pay for the operation of these programs; and (6) RTR questionably allocated $141,478 in nonreimbursable expenses.

We found that between fiscal years 2002 and 2008, RTR provided unnecessary compensation totaling as much as $621,847 to its President and his wife, who was RTR's Vice-President of Development. Specifically, in January 2002, RTR appointed a new Executive Director to oversee its operations. At this time, according to members of RTR's Board of Directors, the President was kept on as an employee, but his job responsibilities were significantly reduced in that he was no longer responsible for the day-to-day operations of RTR. Nevertheless, despite this reduction in responsibility, the President continued to receive his full salary until he left RTR in November 2007. RTR's

Board of Directors also indicated that in November 2006, in anticipation of the President's leaving RTR, his wife was promoted from RTR's Vice-President of Development to Acting Chief Executive Officer (CEO), and her compensation was increased by over 100% from $82,022 to $190,778 annually, which she received until she left RTR in November 2007. According to members of RTR's Board of Directors, the Vice-President of Development was promoted to this position and had her compensation significantly increased in an attempt to keep the incorporators (RTR's President and his wife) "whole" by keeping their combined earnings at approximately the same level as it was prior to the President's removal from RTR's payroll system. However, at the time the Vice-President of Development was promoted, RTR was paying a full-time Executive Director who had been appointed in 2002 to oversee the operations of RTR. Moreover, as noted in the Background section of this report, at the time of the promotion, the President and his wife had significant control over RTR's board. Accordingly, there is inadequate assurance that RTR's board was able to make decisions relative to the compensation to these individuals in an independent manner.

We found that during our audit period, RTR had not established formal written procurement policies or procedures. Moreover, we found that during fiscal year 2004, contrary to state regulations and without the knowledge or consent of RTR's Board of Directors, RTR's President noncompetitively awarded a $1.6 million construction contract to a relative of a member of RTR's Board of Directors to perform renovations at RTR's corporate headquarters. Because this contract was awarded on a noncompetitive basis, there is inadequate assurance that RTR obtained the highest-quality services for the lowest price.

Our review revealed that during our audit period, RTR's President and its former Executive Director selectively provided fringe benefits totaling $26,299 to certain staff members that were in excess of what is allowed by RTR's policies and procedures. According to state regulations, fringe benefits such as these that are not available to all employees under an established agency policy are nonreimbursable under state-funded contracts.

During our audit, we identified a number of areas in which RTR needed to improve its administration of its personnel activities. Specifically, although RTR had a policy that required all agency staff to complete individual timesheets documenting the number of hours worked by each staff person in each program, during our audit period at least 11 of RTR's administrative employees were not required to complete these time records in this manner. We also found that only one personnel file of these 11 staff members contained a formal job description indicating the employee's job-related responsibilities. Further, contrary to the terms and conditions of RTR's state contracts, there was no evidence that RTR's board ever formally evaluated the performance of its Executive Director. In fact, only one the 11 staff members in our sample (RTR's Vice-President of Finance) had any evidence of receiving a performance evaluation during the entire audit period. As a result, there is inadequate assurance that all of the salary-related compensation of these 11 employees, which totaled $3,032,646 during fiscal years 2005 through 2008, was properly allocated to RTR's state-funded contracts. Further, by not establishing formal job descriptions for these positions and not conducting regular performance evaluations, RTR lacked adequate controls over its administrate staff to establish appropriate accountability for their administrative activities or criteria against which these staff members could be evaluated.

We found that during our audit period, RTR provided full-time equivalent (FTE) staffing in two of its residential programs that was significantly lower (between 26% and 44%) than what was required by the state contracts that funded these programs. As a result of its not being able to provide the required FTE program staff, RTR had to pay overtime compensation that was between 218% and 812% above what was approved by DMR in the contracts that funded these two programs and also hire relief staff to provide the required level of services in these two programs. In one instance, these excessive overtime expenses resulted in DMR's having to agree to amend the contract that funded one of these two programs and provide RTR with an additional $80,749 to cover program deficits. Further, given that a significant amount of the program services in these two programs was provided by overtime and relief staff rather than through the required level of FTE staff, there is inadequate assurance that the quality of the services provided by RTR in these programs during our audit period was in compliance with RTR's contracts with DMR.

During fiscal year 2007, RTR allocated all of its reported nonreimbursable administrative expenses, which totaled $141,478, to only one of its federally funded programs rather than allocating these costs to all of its programs using an acceptable cost allocation plan as required by Operational Services Division (OSD) regulations. This questionable allocation resulted in RTR's being able to expense this entire $141,478 in administrative nonreimbursable expenses, of which $101,997 otherwise would have been subject to recoupment by the Commonwealth had they been properly allocated to RTR's state-funded programs.

During the course of our audit, we identified one other issue, which although did not involve instances of noncompliance to specific laws, regulations, policies, procedures, or contractual terms and conditions as the ones detailed above, did have an impact on the financial viability of RTR. Consequently, we are disclosing this issue to RTR's management for its consideration.

Sound business practices advocate that entities such as RTR evaluate their performance and take the measures necessary to ensure that they operate in the most efficient and effective manner. However, we found that during our audit period RTR's community services Venture Program incurred significant financial losses, and the costs of its fundraising activities exceeded the revenue collected. Moreover, RTR did not appear to make any changes in either of these activities to improve their efficiency.

INTRODUCTION

Background

Road to Responsibility, Inc., (RTR) was incorporated in November 1988 as a private, nonprofit corporation to provide residential, social, vocational, recreational, counseling, and educational services to individuals with mental and other disabilities who reside in Southeastern Massachusetts. RTR employs approximately 400 individuals and maintains its headquarters at Library Plaza in Marshfield.

During the period covered by our audit, RTR was providing services to more than 1,000 clients in 19 programs, of which 18 received state funding. These programs include employment and training (day workshops), residential, day habilitation and Venture Program (community outreach) work and recreation programs. In its employment and training programs, RTR teaches mentally handicapped individuals vocational, employment, and other educational skills to prepare them to work in a more independent, supported work environment. In its residential programs, RTR teaches mentally handicapped and/or multi-handicapped individuals independent living skills and provides them with residential services. In its day habilitation programs, RTR provides clients recreational opportunities and opportunities to develop social skills in a group environment. In the Venture Program, RTR provides leisure and work opportunities for disabled adults in a supervised setting.

During fiscal years 2005, 2006, and 2007, RTR received funding from a variety of sources, as indicated in the following table:

Summary of Revenue

Revenue Sources	Fiscal Year 2005	Fiscal Year 2006	Fiscal Year 2007
Contributions	$237,639	$329,803	$156,347
Gov. In-Kind/Capital Budget	58,952	100,500	33,356
Private In-Kind	61,403	200,940	23,211
Other Grant	0	0	7,750
Dept. of Mental Health	50,155	97,089	101,355
Dept. of Mental Retardation	13,737,127	14,660,699	15,657,476
Dept. of Social Services	126,808	128,578	0
Dept. of Transitional Assistance	54,435	120,362	145,370
Mass. Comm. for the Blind	0	15,034	15,034
Mass. Rehabilitation Commission	317,522	414,778	401,541
Other Mass. State Agency-POS	0	211,731	283,515
Mass. State Agency Non-POS	183,995	0	0
Direct Federal Grants/Contracts	57,450	55,049	35,908
Medicaid-Direct Payments	2,790,019	3,293,120	3,570,677
Client Resources	1,047,021	1,039,608	1,150,834
Private Client Fees	55,587	55,702	47,844
Commercial Activities	847,288	824,748	957,721
Investment Revenue	10,385	2,847	27,809
Other Revenue	74,251	558,915	14,456
Released Net Assets-Program	3,032	3,061	11,781
Released Net Assets-Time	91,945	139,102	75,816
Total	$19,805,014	$22,251,666	$22,717,801

During the period covered by our audit, the structure of RTR's Board of Directors limited its ability to meet its oversight responsibilities in an independent manner. Specifically, RTR's corporate structure was organized in such a way that RTR's incorporators were considered "Charter Members" of the corporation and empowered to control the size, composition, election, and termination of the members of RTR's Board of Directors. However, the incorporators were RTR's President and his wife, who was RTR's Vice-President of Development. Therefore, it was clearly not possible for RTR's board to fully meet its responsibility to independently oversee the activities of RTR, including evaluating the activities of RTR's President and his wife, since these two individuals had the authority to remove board members from their position on the board without cause. At its December 12, 2007 meeting, over the objection of the Charter Members, RTR's board voted to modify its corporate bylaws to remove its Charter Members. This termination of corporate membership was reflected in Article I of RTR's bylaws as modified on December 12, 2007, as follows.

> *The Corporation is a corporation without corporate members.*

Although RTR's board has taken measures to address this issue, during the period covered by our audit it was not constituted in such a manner that would allow it to perform all of its oversight responsibilities in an independent manner. Consequently, we believe that many of the issues detailed in our report are partly the result of the board's inability to fully and independently meet all of its oversight responsibilities.

Audit Scope, Objectives, and Methodology

During fiscal year 2008, the Office of the State Auditor (OSA) received information that raised concerns about certain activities of RTR and its administrative staff. As a result of these concerns, and in consultation with RTR's principal state purchasing agency, the Department of Mental Retardation (DMR), the OSA initiated an audit of RTR. The scope of our audit was to examine various administrative and operational activities of RTR during the period July 1, 2004 to December 31, 2007.

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 that provides 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.

Our audit objectives consisted of the following:

- A determination of whether RTR had implemented effective internal controls, including:
  1. Processes for planning, organizing, directing, and controlling program operations;

2. Policies and procedures to ensure that resource use is consistent with Massachusetts laws and regulations; and

3. Policies and procedures to ensure that resources are safeguarded and efficiently used.

- An assessment of RTR's business practices and its compliance with applicable laws, rules, and regulations, as well as the various fiscal and programmatic requirements of its state contracts.

In order to achieve our objectives, we first assessed the internal controls established and implemented by RTR over its operations. The purpose of this assessment was to obtain an understanding of management's attitude, the control environment, and the flow of transactions through RTR's accounting system. We used this assessment in planning and performing our audit tests. We then held discussions with RTR officials and reviewed organization charts; internal policies and procedures; and all applicable laws, rules, and regulations. We also examined RTR's financial statements, invoices, and other pertinent financial records to determine whether expenses incurred under its state contracts were reasonable; allowable; allocable; properly authorized and recorded; and in compliance with applicable laws, rules, and regulations. Finally, we conducted additional audit testing in those areas where concerns had been raised in the information received by the OSA.

As noted in the previous table, RTR receives both Commonwealth funds as well as a significant amount of funding from other governmental and private sources. For the purposes of our report, we disclosed any deficiencies we identified involving state funds in the Audit Results section of this report. However, in order to fully disclose the results of our audit work, we included in the Other Matters section of this report any deficiencies we identified in areas that did not involve instances of noncompliance with state laws regulations or the terms and conditions of state contracts. These other matters are being reported on for the purposes of bringing them to management's attention, which we believe could have a significant impact on RTR's operations.

Our audit was not made for the purposes of forming an opinion on RTR's financial statements. We also did not assess the quality and appropriateness of all program services provided by RTR under its state-funded contracts. Rather, our report was intended to report findings and conclusions on the extent of RTR's compliance with applicable laws, rules, regulations, and contractual agreements, and to identify services, processes, methods, and internal controls that could be made more efficient and effective.

At the conclusion of our audit fieldwork, a draft copy of this audit report was provided to RTR officials for review and comments. In response, RTR and a representative of its private accounting firm provided specific comments to each of the audit results contained in our report. In addition, RTR officials provided some general comments, which are excerpted below:

In the fall of 2007, a series of events had given rise to the Board of Directors of Road to Responsibility to take several decisive, and in hindsight, overdue actions to address organizational and operational matters that threatened the agency's future. The process started when members of the agency's senior management team, including the Executive Director, brought concerns about financial and personnel matters of the company to the Board. As the Board was dealing with these issues, anonymous complaints to the State Department of Mental Retardation and the Quincy Patriot Ledger raised similar questions about RTR's financial and personnel practices. This resulted in a series of highly visible, unfavorable newspaper articles as well as a two-pronged increase in state agency oversight by the State Auditor's Office and the Department of Mental Retardation.

As these events were occurring, the Board of Directors appointed an interim CEO and began a yearlong, intensive process of working closely with both the Department of Mental Retardation and the State Auditor's Office to correct root causes and establish revised policies to address the shortcomings of its past practices.

It cannot be overstated that the fundamental weakness in RTR's internal controls stemmed from a lack of executive accountability brought about by RTR's flawed governance structure. The organization's governing body was structured in such a way that two married employees held the top management positions within the organization, and, as Members, had exclusive control of its governing body. By taking the steps necessary to remedy this situation, the Board of Directors was able to affirmatively restore the integrity and priorities of the organization.

Over the past year, changes have occurred within the Agency to ensure that the problems identified in the Audit Report never reoccur. A brief summary of what RTR's new leadership has done over the past year provides an essential context to the deficiencies identified to have occurred during the preceding two and one-half years that the audit covers.

At the Board of Directors meeting of 10/31/07 the board adopted a sweeping corrective action plan that put in motion the following actions:

- *The RTR Board took all steps necessary and completed all required filings to change its governance structure from its former Member structure to a self-perpetuating Board of Directors.*
- *In November 2007 12 administrative staff were laid off and/or terminated thereby substantially streamlining its administrative operations.*
- *The agency eliminated all non-performing "venture" programs and sold all non-performing assets.*
- *The agency has adopted comprehensive policies governing Personnel Practices, Fringe Benefits and Internal Controls, in particular adopting policies requiring competitive bidding for purchasing and contracting and specifically prohibiting related party transactions.*

As evidenced by these steps already taken by RTR, and acknowledged in the State Auditor's Report, there is no disagreement with three of the State Auditor's six findings (findings 2, 3 and 4) as well as the comments regarding the operations of the "ventures" programs and fundraising activities. We firmly believe that the corrective actions, already taken, will assure that none of the Auditor's findings will ever recur. . . .

Although we disagree with . . . [the three remaining] isolated findings, three important truths emerge:

- *We acknowledge the errors in the past.*
- *We have corrected those errors decisively and effectively.*
- *We humbly and proudly continue to provide excellent care to more than a thousand of the Commonwealth's most vulnerable citizens.*

AUDIT RESULTS

1. UNNECESSARY EXECUTIVE COMPENSATION TOTALING AS MUCH $621,847

We found that between fiscal years 2002 and 2008, Road to Responsibility, Inc., (RTR) provided unnecessary compensation totaling as much as $621,847 to its President and his wife, who was RTR's Vice-President of Development. Specifically, in January 2002, RTR appointed a new Executive Director to oversee agency operations. At this time, according to members of RTR's Board of Directors, the President was kept on as an employee, but his job responsibilities were significantly reduced in that he was no longer responsible for the day-to-day operation of RTR. Nevertheless, despite this reduction in responsibility, the President continued to receive his full salary until he left RTR in November 2007. RTR's Board of Directors also indicated that in November 2006, in anticipation of the President's leaving RTR, his wife was promoted from Vice-President of Development to Acting Chief Executive Officer (CEO) of RTR, and her compensation was increased by over 100% from $82,022 to $190,778 annually, which she received until she left RTR in November 2007. According to members of RTR's Board of Directors, the Vice-President of Development was promoted to this position and had her compensation significantly increased in an attempt to keep the incorporators (RTR's President and his wife) "whole" by keeping their combined earnings at approximately the same level as they were prior to the President's departure from RTR. However, at the time the Vice-President of Development was promoted, RTR was paying a full-time Executive Director who had been appointed in 2002 to oversee the operations of RTR. Moreover, as noted in the Background section of this report, at the time of the promotion, the President and his wife had significant control over RTR's board. Accordingly, there is inadequate assurance that RTR's board was able to make decisions relative to the compensation to these individuals in an independent manner.

The state's Operational Services Division (OSD), the state agency responsible for regulating and overseeing the activities of all contracted human service providers, such as RTR, has defined what constitutes reasonable operating costs under state contracts in its regulations 808 CMR 1.02, as follows:

> *<u>Reimbursable Operating Costs</u>. Those costs reasonably incurred in providing the services described in the contract. . . . Operating costs shall be considered "reasonably incurred only if they are reasonable and allocable using the standards contained in Federal Office of Management and Budget Circular A-122 or A-21, or successors thereto.*

The Office of Management and Budget (OMB) Circular A-122 defines reasonable costs as follows:

> *Reasonable costs. A cost is reasonable if, in its nature or amount, it does not exceed that which would be incurred by a prudent person under the circumstances prevailing at the time the decision was made to incur the costs. . . . In determining the reasonableness of a given cost, consideration shall be given to:*
>
> *Whether the cost is of a type generally recognized as ordinary and necessary for the operation of the organization or the performance of the award.*
>
> *The restraints or requirements imposed by such factors as generally accepted sound business practices, arm's length bargaining, Federal and State laws and regulations, and terms and conditions of the award.*
>
> *Whether the individuals concerned acted with prudence in the circumstances, considering their responsibilities to the organization, its members, employees, and clients, the public at large, and the Federal Government . . . .*

Moreover, OSD regulations 808 CMR 1.05 indicate that contract funds can only be used for reasonable costs as defined by OMB Circular A-122, as follows:

> *Funds received from Departments may only be used for Reimbursable Operating Costs as defined in 808 CMR 1.02. In addition, funds may not be used for costs specifically identified in 808 CMR 1.05 as non-reimbursable.*

Further, Section 1 of these regulations specifically identifies the following as nonreimbursable costs against state contracts:

> *(1) Unreasonable Costs. Any costs not determined to be Reimbursable Operating Costs as defined in 808 CMR 1.02 or any amount paid for goods or services which is greater than either the market price or the amount paid by comparable Departments or other governmental units within or outside of the Commonwealth.*

As noted in the Background section of this report, during the period covered by our audit, RTR's President and his wife had such significant control over RTR's Board of Directors that it hindered the board's ability to perform all of its responsibilities in an independent manner. Given this internal control issue, we analyzed the compensation provided to RTR's President and his wife during the period covered by our audit. Our review revealed that these two individuals were provided with salaries totaling $1,039,511 during this period, as indicated in the table below:

Fiscal Year	President	Vice-President of Development
2004	$151,164	$73,846
2005	163,280	75,955
2006	162,510	80,222
2007	82,065	129,293
2008*	0	121,176
Total Compensation	$559,019	$480,492

* Information was extracted from RTR's payroll records because RTR's 2008 Uniform Financial Statement and Independent Auditor's Report (UFR) had not been filed as of our report date. Both employees were terminated on November 5, 2007. The Vice-President of Development's 2008 salary includes $48,096 in vacation buyback upon termination.

On January 1, 2002, RTR appointed one of its staff members to the position of Executive Director of RTR with an annual salary of $140,578. According to a member of RTR's Board of Directors, this was done so that RTR's President would be relieved from dealing with the day-to-day operation of RTR. This board member stated that at this time the President's role was reduced from overseeing the day-to-day operations of RTR to still doing work in the community, running RTR's Venture Program, and conducting fundraising activities. However, as noted in the previous table, although the President's job-related responsibilities were significantly reduced, he did not receive any corresponding reduction in his salary until he left RTR in November 2006. Because RTR hired a full-time Executive Director in January of 2002 who assumed many of the President's job related responsibilities but did not reduce the President's compensation, we believe that as much as $773,442 in salary that RTR provided to its President between January 1, 2002 and November 2007 was excessive and unnecessary, of which as much as $519,532 was charged to the Commonwealth, as detailed in the following table:

President's Unnecessary Compensation

Fiscal Year	Salary	Nonreimbursable Expenses**	Adjusted Salary
2002*	$66,147	$6,572	$59,575
2003	148,277	25,911	122,366
2004	151,164	22,983	128,181
2005	163,280	30,603	132,677
2006	162,510	88,662	73,848
2007	82,065	79,180	2,885
2008	0	0	0
Total Salary:	$773,443	$253,911	$519,532

* This figure is based on six months of salary from fiscal year 2002, since action happened half way through the fiscal year.

** These amounts were identified by RTR as being nonreimbursable expenses in the financial statements that RTR filed with the Commonwealth and were not directly charged against state contracts.

Further, in November 2007, the President's wife, who was functioning as RTR's Vice-President of Development, was appointed by the board to be RTR's Acting Chief Executive Officer (CEO), and at this time her salary was increased by over 100% from $82,022 to $190,000. According to a member of RTR's Board of Directors, this was done in an attempt to keep the incorporators "whole" by keeping their combined earnings approximately the same in anticipation of the President going off the payroll. However, it should be noted that the President was not removed from RTR's payroll system until October 28, 2007 and continued to receive some sort of compensation, primarily in the form of accrued vacation and sick time compensation, until March 18, 2007.

During our audit, we asked members of RTR's Board of Directors what additional responsibilities the Vice-President of Development assumed in her new position as Acting CEO, since there was no written job description or stated duties for this new position. These board members stated that they were unsure and that her job responsibilities were to be worked out by the President and RTR's Executive Director. Based on the fact that at this time RTR already had a full-time Executive Director, and on the statements made by a member of RTR's Board of Directors that the Vice-President of Development's pay was increased solely to keep her and her husband's compensation at a certain level, we believe that the difference between her original salary of $82,022 and her salary increase to the position of Acting CEO from the time she was promoted until the time she left RTR in November 2007 was unnecessary. The following table identifies the unnecessary and questionable salary provided to this individual during the period covered by our review:

Unnecessary Acting CEO Compensation

Fiscal Year	New CEO Salary	Old Salary	Nonreimbursable Expenses	Variance
2007*	$91,350	$37,140	$23,805	$30,405
2008	73,080	29,712	N/A	43,368
2008 Vacation Buy-Back (526.5 hrs)	48,096	19,554	N/A	28,542
Total	$212,526	$86,406	$23,805	$102,315

* The actual increase in this individual's pay went into effect on January 1, 2007, which was half way through fiscal year 2007. Consequently, the salary figures show are what she received for the second half of fiscal year 2007, when her new salary was in effect, through the date on which she left during fiscal year 2008.

Based on our review of agency records we noted several other problems with the compensation provided to these two individuals, as follows:

- These two individuals filled out a different attendance records/timesheets than was required under RTR guidelines, and this record did not identify the specific functions benefited or the work performed (see Audit Result No. 4). Furthermore, on several occasion these employees approved their own timesheets. As a result, there is inadequate assurance that these timesheets accurately reflect the work that may have been performed by these individuals.

- In April 2004, the President and his wife moved to New Hampshire and, according to agency staff, were rarely seen in the RTR office. Although we acknowledge that it would be possible for the President and his wife to perform job-related actives from their home, there was no formal written board approval for them to work out of their home, and the board did not develop any specific job-related responsibilities or reporting requirements for these two individuals while they were living and working out of their New Hampshire home. Consequently, it was not possible to assess the level of any job-related activities conducted by these two individuals during this period of time.

In an April 7, 2004 letter to the Board of Directors, the President stated the following regarding this move:

> *[My wife] and I have bought a new home. Given some personal issues and the absurdity of the local real estate market, we chose a home in Andover, New Hampshire . . . . My plan will be to commute, staying in Marshfield Monday through Thursday at an unsold room in one of our motels . . . . [My wife] will shift to a different position heading our much-needed grant writing effort. She will be very difficult to replace as our head of development. . . . Everything becomes possible when family is the motivator.*

During our audit, we asked members of RTR's Board of Directors if they were aware of the arrangement the President cited in his April 7, 2004 letter that involves him commuting from New Hampshire and staying in a room in a motel owned by RTR. In response to our inquiry, the board members stated that they were aware of the President's move to New Hampshire but were not sure if he ever stayed at the motel in question. These board members added that, to their knowledge, the President only commuted for a short time before he was injured and went out on disability. Further, RTR's CEO stated that the President and his wife were only required to be present at RTR a few days a month when they lived out of state.

Recommendation

As noted above, the two RTR individuals in question received as much as $899,563 ($773,443 for the President and $126,120 for the Acting CEO) in unnecessary compensation. However, RTR identified $277,716 of these salary expenses as being nonreimbursable in its UFRs. Consequently, in order to address our concerns relative to this matter, we recommend that RTR, in collaboration with the Department of Mental Retardation (DMR), determine what amount of the remaining $621,847 was nonreimbursable. At a minimum, this amount should include the $102,315 in increased compensation provided to RTR's Acting CEO that was not identified as being nonreimbursable to the Commonwealth during the audit period. RTR should then amend its fiscal years 2002 through 2007 UFRs as necessary and correctly file its 2008 UFR to identify the unnecessary compensation expenses as being nonreimbursable to the Commonwealth. If RTR does not have sufficient non-state funds to pay for these nonreimbursable salary expenses, then DMR should take whatever measures it considers necessary, including recoupment of these funds, to resolve this matter. In the future, RTR's board should not provide any compensation to staff members that is not necessary to effectively and efficiently run RTR.

Auditee's Response

In response to the audit result, RTR officials provided the following comments:

It is our contention that the findings here reflect a misunderstanding about the structure and responsibilities of the President/CEO and the Executive Director at RTR during the audit period. These apparent misunderstandings led to the State Auditor's Office (SAO) to conclude that 100% of the President's compensation from mid-2002 through 2007 was unnecessary, as was a portion of the acting CEO's compensation in 2007 and 2008 upon receiving a substantial pay increase. The apparent misunderstanding is the assumption by the SAO that, because of the presence of the 'Executive Director' that the continued presence of a 'President/CEO' was duplicative. The President/CEO and acting CEO had long been integral to the organization as well as being well-recognized and respected members of their community, thereby providing numerous connections to RTR's supporters and vendors. As can be clearly seen from the organizational chart dating back to the audit period, the President/CEO and acting CEO maintained significant day-to-day responsibilities within the agency while also emphasizing the cultivation of external relationships for the corporation. In particular, the President/CEO was responsible for the supervision/oversight of the Finance, Human Resources, Fundraising, Quality Assurance and Ventures operations. Evidence of this continual involvement is noted in the numerous contractual documents enacted during this period along with documentation evidencing fundraising activities. The Executive Director, on the other hand, had supervisory oversight responsibilities over the Residential, Employment/Work and Day Habilitation services provided by the agency. In an agency the size of RTR, Inc., it is quite common to have a division of labor at the top of the management hierarchy similar to this, though frequently, the role played by the 'Executive Director' here is identified as either the 'Chief Operating Officer' or the 'Deputy Director.' RTR made efforts to carefully separate reimbursable vs. non-reimbursable salary expenses and there were sufficient accumulated surplus derived from non-Commonwealth sources available as an offset.

Changes Made to Correct this Potential Issue:

- *The 'Executive Director' position has been eliminated.*
- *A new policy governing how salaries for highly paid employees. . . has been enacted.*
- *We will re-file past UFRs if warranted to better reflect non-reimbursable expense.*

In addition, a representative from RTR's private accounting firm provided the following comments:

The State Auditor's Office (SAO) has taken the position that 100% of the President's compensation from mid 2002 through 2007 was unnecessary, as was a portion of the acting CEO's compensation in 2007 and 2008 upon receiving a substantial pay increase. From our perspective as external auditors, the President and acting CEO had long been integral to the organization and were recognized and well-respected by their peers and as members of their community, thereby providing numerous connections to RTR's supporters and vendors. Evidence of their continued presence is noted throughout the many contractual documents as well as documentation evidencing fundraising activities. While the manner in which their services were provided and the specific hours contributed may not have always been readily identifiable according to SAO, RTR's Board of Directors clearly recognized value in their continued employment and provided compensation thought to be consistent with industry norms. While the necessity of this *compensation cost may be debatable, should OSD determine that these costs should be considered nonreimbursable, RTR does have a sufficient accumulated surplus derived from non-Commonwealth sources available as an offset.*

Auditor's Reply

Contrary to RTR's assertion, we do understand the structure and responsibilities of the President and the Executive Director of RTR during our audit period. Our report clearly acknowledges the fact that when RTR hired the Executive Director in question, RTR's President still maintained responsibility for overseeing some agency-related activities. However, since we were not provided with any agency records that identified what specific responsibilities the President would be responsible for, we relied on the representations made to us by a member of RTR's Board of Directors as to the job-related activities the President performed during the period in question. Based on these representations and RTR's own admission, the President's job responsibilities were significantly reduced without any decrease in compensation. Moreover, contrary to the assertion of RTR's private accounting firm, we do not take issue with 100% of the compensation provided to RTR's President. Based on our discussions with RTR staff and board members, a number of the tasks performed by the President were integral to the agency's successful operation. However, based on the information we were able to obtain during our audit as discussed above, we believe that it is both reasonable and prudent for us to question the necessity of some of the compensation provided to this individual during the audit period.

In its response, RTR states that there was documentation evidencing fundraising activities conducted by this individual. However, this assertion conflicts with the fact that none of the costs associated with this President's compensation was expensed to fundraising in the UFRs that RTR provided to the Commonwealth, which therefore calls into question the extent he actually performed fundraising activities. Moreover, as noted in our report, the President was not required to fill out time and attendance records that indicated the function benefited or the work performed in accordance with state regulations and RTR policy. Therefore, it was not possible to determine with reasonable assurance the work that was actually performed by this individual during the audit period.

In its response, RTR states, "In an agency the size of RTR, Inc., it is quite common to have a division of labor at the top of the management hierarchy similar to this, though frequently, the role played by the 'Executive Director' here is identified as either the 'Chief Operating Officer' or the 'Deputy Director'." Although we do not dispute that management within an agency should be properly staffed, there was no indication in the minutes of RTR's Board of Directors indicating that the board had made a determination regarding a definite need for this additional management position. The need for this additional management position is also questionable given that, once the President resigned, RTR did not fill and has now eliminated the position of Executive Director. It is the responsibility of an agency's Board of Directors to establish the compensation level for its chief executive based on his or her duties, responsibilities, and job performance. As previously mentioned, upon hiring an Executive Director, the former President's responsibilities were clearly reduced without any decrease in his compensation. Moreover, the extent of the President's job-related responsibilities could not be determined because RTR did not develop a job description that documented his responsibilities, and RTR's board did not formally establish his new responsibilities in writing so that it could adequately assess his performance.

In its response, RTR does not take issue with our questioning of the reasonableness of the compensation provided to the Acting CEO. Accordingly, it is clear that this compensation was unnecessary and excessive and should not have been charged to state contracts.

We recognize that RTR has taken measures to address our concerns relative to this issue, and we believe that such measures were both necessary and responsive to our concerns in this matter.

2. NONCOMPETITIVE AWARDING OF $1.6 MILLION CONSTRUCTION CONTRACT BY RTR'S PRESIDENT

We found that during our audit period, RTR had not established formal written procurement policies or procedures. Moreover, we found that during fiscal year 2004, contrary to state regulations and without the knowledge or consent of RTR's Board of Directors, RTR's President noncompetitively awarded a $1.6 million construction contract to a relative of a member of RTR's Board of Directors to perform renovations at RTR's corporate headquarters. Because this contract was awarded on a noncompetitive basis, there is inadequate assurance that RTR obtained the highest-quality services for the lowest price.

The 808 CMR1.03 (8), promulgated by OSD, establishes the following competitive procurement requirements that all contracted human service providers such as RTR must follow:

> *All procurements of furnishings, equipment and other goods and services by or on behalf of a Contractor shall be conducted in a manner to provide, to the maximum extent practical, open and free competition. Capital Items as defined in 808 CMR 1.02, shall be acquired through solicitation of bids and proposals consistent with generally accepted accounting principles.*

Despite this requirement, we found that on October 14, 2003, RTR's President noncompetitively awarded a contract to Pyne Construction (Pyne) of Boston to renovate RTR's corporate headquarters in Marshfield. Under the terms and conditions of this contract, Pyne was to provide construction management services for the renovation of approximately 12,000 square feet of office space for RTR. In return for these services, RTR agreed to pay Pyne a fixed fee of $90,000 plus the cost of construction work done by the company or any of its subcontractors. The total cost of this project when completed was $1,664,762.

RTR's President informed RTR's Board of Directors of his decision to award this contract on a noncompetitive basis in an Oct. 20, 2003 letter, in which he stated, in part:

> *On Tuesday 14 Oct 03 I engaged the services of Ted Pyne Construction as construction manager for our Library Plaza building project. I made this decision with no input from the Board of Directors. . . . I solicited no other bids because Ted is not charging for his personal time on the project. . . .*

Because RTR's President awarded this contract without the benefit of a competitive procurement process and without the prior knowledge and consent of RTR's full Board of Directors, there is inadequate assurance that RTR obtained the best services at the lowest possible cost for these services. Also, the President's reason for hiring this company, as expressed in his October 20th letter to RTR's Board, in our opinion is not valid since the company received a fixed fee of $90,000 and additional hundreds of thousands of dollars for services it provided under the contract.

During our audit, we brought this matter to the attention of some members of RTR's Board of Directors. One member informed us that his brother owned the company selected by the President but that he was not involved in the decision-making process. Further, the board member noted that, since this procurement was made without formal Board of Directors approval, he never had an opportunity to vote or formally give his opinion on this matter.

As a result of our audit, RTR officials developed a new written policy regarding the procurement of goods and services, stating the following:

> *RTR will obtain at least three independent bids and/or proposals for contracts and/or services purchased from third parties when the amount of such engagements exceeds $1,000 for an individual project, or when said contractor will be used on a revolving, open order basis. All procurements will be subject to the agency's Related Party Policy.*

Recommendation

As noted above, during our audit fieldwork, RTR developed formal written procurement policies and procedures. Such measures were necessary and appropriate, and we recommend that RTR take the measures necessary to ensure that these policies and procedures are adhered to for all future procurements.

Auditee's Response

In response to the audit result, RTR officials stated, in part:

> *We do not disagree with the overall finding in this area.*
>
> *Changes Made to Correct this Issue:*
>
> - *A policy has been enacted to our accounting manual that calls for a competitive bid process being required for any purchases greater than $5,000.*
> - *A 'Related Party' policy has been established.*

In addition, a representative from RTR's private accounting firm provided the following comments:

> *The SAO has indicated that RTR had no formal written procurement policies or procedures and that RTR's President non-competitively awarded a $1.6 million construction contract to a relative (brother) of a member of RTR's Board of Directors. In fact, RTR did have formal policies in place, and the accounting manual provided to RTR's external auditors in October of 2003, under "Account's Payable – Purchasing" item #4 states "any purchase of goods or services from a "related party" (Board member, employee, or relative of either) must be approved by the President." Additionally, the Board was advised by letter within six days of engaging Ted Pyne Construction to serve as project manager for a fixed fee of $90,000. The Board certainly had the opportunity to ratify or object to this arrangement.*
>
> *The competitive procurement regulations applicable to this transaction state the following:*
>
> *"All procurements of furnishings, equipment and other goods and services by or on behalf of a Contractor shall be conducted in a manner to provide, to the maximum extent practical, open and free competition. Capital Items as defined in 808 CMR 1.02, shall be acquired through solicitation of bids and proposals consistent with generally accepted accounting principles."*

It was the President's position that further solicitation of bids was not practical in this circumstance given the willingness of a related party to serve as project manager for a fair fixed fee during a period when construction services were at an all-time high and price gouging by construction contractors had become the norm. The objective behind hiring a project manager was to ensure that the project was completed at the lowest possible cost. It was believed that the project manager was significantly more capable of curtailing costs than RTR management would be, given his expertise in the construction industry.

Auditor's Reply

It its response, RTR states that it agrees with the issue presented in this Audit Result and has taken measures to address this matter. We believe the actions taken by RTR relative to this issue were necessary and responsive to our concerns in this area.

Regarding the response provided by the official from RTR's private accounting firm, the representative states "RTR did have formal policies in place, and the accounting manual provided to RTR's external auditors in October of 2003, under "Account's Payable – Purchasing" item #4 states "any purchase of goods or services from a "related party" (Board member, employee, or relative of either) must be approved by the President." However, as stated in our report, RTR officials did in fact confirm with us that during our audit period RTR did not have a formal policy relative to the procurement of goods and services. This assertion is supported by the fact that RTR, subsequent to our bringing this mater to its attention, did develop and implement such a policy. Further, it appears that, based on his comments, the representative from RTR's private accounting firm believes this statement constitutes an adequate procurement policy. However, in our opinion, this statement does not in any way constitute a policy that provides adequate internal controls over RTR's procurement process since it does not cover all types of procurements, including those from non-related-party entities, does not establish standard competitive procurement guidelines such as dollar values applicable to competitive procurements, or specify solicitation procedures. Rather, this statement appears to be merely an accounting guide rather than an official procurement policy formally adopted by RTR. Further, from an audit perspective, this statement is concerning given that it is not consistent with OSD regulations and that, during this period of time, RTR's former President had significant control over RTR's Board of Directors. Accordingly, proper controls and accountability over RTR's procurement activity had not been established.

In its response, the representative from RTR's private accounting firm states, "Additionally, the Board was advised by letter within six days of engaging Ted Pyne Construction to serve as project manager for a fixed fee of $90,000. The Board certainly had the opportunity to ratify or object to this arrangement." Our report clearly acknowledges the fact that RTR's former President informed RTR's board that he had noncompetitively awarded the contract in question. However, since the board was not notified of this until after the former President had executed a legally binding contract with the aforementioned company, we question what measures, including objecting to the agreement, the board could have taken. Also, as can be seen from the October 20th letter, the former President was merely informing the board of his decision and was not seeking their input on the matter. Clearly, since this was not an emergency situation, the former President had sufficient time to either conduct a proper competitive procurement for this contract and to present this matter to RTR's board for its opinion before he entered into this contract.

Moreover, during our audit, we were not provided with any record that documented why RTR's former President chose to noncompetitively award this contract other than the aforementioned October 20, 2003 letter. As noted above, in this letter, the former President stated that he chose this company because its owner was not going to charge for its time on the project. Contrary to the assertion of the official from RTR's private accounting firm, the former President made no reference to any belief that further solicitations were not practical because he had concluded that construction costs "were at an all time high and price gouging by construction contractors was the norm." Clearly the former President if he so chose, had the time to use a competitive procurement process in this matter. We do not question the potential value of having a project manager oversee a project of this type. However, RTR may have been able to realize some cost savings had the former President chose to solicit competitive bids for the project management and related construction services.

3. UNALLOWABLE BONUS AND FRINGE BENEFITS TOTALING AT LEAST $26,299 PAID TO SELECTED RTR EMPLOYEES

Our review revealed that during our audit period, RTR's President and its former Executive Director selectively provided fringe benefits totaling $26,299 to certain staff members that were in excess of what is allowed by RTR's policies and procedures. According to state regulations, fringe benefits such as these, which are not available to all employees under an established agency policy, are nonreimbursable under state-funded contracts.

The 808 CMR 1.05 (9), promulgated by OSD, identifies the following as being nonreimbursable expenses under state contracts:

> *Certain Fringe Benefits. Fringe benefits determined to be excessive in light of salary levels and benefits of other comparable Contractors and fringe benefits to the extent that they are not available to all employees under an established policy of the Contractor . . . .*

Furthermore, the UFR Auditor's Compliance Supplement, promulgated by OSD, provides additional guidance regarding fringe benefits and bonuses, as follows:

> *To be reimbursable, fringe benefits must be available to all employees under an established written policy (in accordance with GAAP) of the Contractor and must not be excessive in comparison to salary and benefit levels of other similar Contractors.*
>
> *There are two ways to furnish bonuses to employees: one is a fixed bonus as part of an employee's salary based on terms incorporated into his or her written employment agreement, and the second is through a Contractor's written employee morale, health and welfare policy, which makes available bonuses to all employees based on exceptional employee performance.*

During our audit of RTR employee personnel files, we noted that RTR's President and its former Executive Director during our audit period selectively provided fringe benefits to certain RTR employees that exceeded those established by RTR's policies and procedures and without formal board approval. Specifically, RTR's vacation policy that was in effect during our audit period provides for agency staff to receive the following vacation leave benefits:

For Staff hired before July 1, 2000

The amount of vacation time given per year is determined by the number of years of service and job classification.

Vacation time accrues in monthly increments as follows:

Years of Service	***Days per Year***
up to 3 completed years	*10*
from 3rd anniversary to 5th completed years	*15*
from 5th anniversary to 10th completed years	*20*
from 10th anniversary	*25*

> ***Effective July 1, 2000, all new hire and/or existing employees who become eligible for benefit time shall accrue and use benefit time as follows:***
>
> *Benefit time can be used for vacation, sick, and/or personal leave*
>
> *The monthly accrual based on a 40 hours work week, shall be as follows:*

Years	***Yearly Accrual***
1-3	*15 days*
3-5	*20 days*
5-10	*25 days*
Over 10	*30 days*

We reviewed the personnel files of a sample of 16 staff members employed by RTR during our audit period and found that, on several occasions, RTR's President or its former Executive Director selectively granted extra vacation time, benefit time, or money to individuals within our sample in excess of the amounts allowed by RTR's written policies, as follows:

a. On February 22, 2005 a letter was sent to RTR's Human Resources Department from RTR's President, stating in part:

> *The [Assistant Vice President of Development] performed extra duties for the first year of the farm with the agreement that I would review the work done and compensate him at that time. I am granting him a one-time payment of $2,500 and two weeks vacation (at his current rate). He may sell back that vacation time if he wishes.*

We found that as a result of this letter, the Assistant Vice-President of Development received a $2,500 bonus and an extra two weeks of benefit time that he accrued throughout our audit period, for an additional liability totaling at least $3,228.

b. On March 29, 2005 RTR's President sent a letter to RTR's Human Resources Department, stating in part:

> *Effective as soon as is convenient for your system [RTR's Executive Director] should accrue vacation at 10 days per year higher then currently.*

We found that as a result of this letter, the former Executive Director was granted 10 days more of vacation per year than the amount allowed by RTR's policies and procedures, which resulted in an additional liability of at least $16,923.

c. On November 23, 2005 a letter was sent to RTR's Human Resources Department from RTR's former Executive Director, stating in part:

> *Please add six days (48 hours) to [RTR's Vice-President of Finance] vacation leave time per our agreement regarding extra days worked . . . .*

d. On June 30, 2006 RTR's former Executive Director sent a letter to RTR's Human Resources Department, stating in part:

> *Please add 16 hours to [RTR's Vice-President of Finance] vacation leave time balance, as of June 30,2006, for that extra time he worked.*

We found that as a result of these letters RTR's Vice-President of Finance was granted an additional six days (48 hours) of vacation time and an additional 16 hours of vacation time on two separate occasions, resulting in an additional liability of at least $3,648.

Since the additional benefits to these individuals were not provided in accordance with RTR's formal written policies and procedures, and because RTR's board had not granted either RTR's President or its former Executive Director the authority to provide these additional benefits, these expenses represent nonreimbursable expenses under RTR's state contracts. The granting of the additional benefit time and compensation to these selected employees created an additional liability to RTR of at least $26,299. It should be noted that during our audit period, these employees either resigned or where terminated from RTR and received all the additional compensation provided to them by the President or former Executive Director either before or at the time of their termination.

During our audit, we brought this matter to the attention of RTR officials, who responded by implementing a new employee benefits policy that prohibits the granting of additional time and compensation to staff beyond the amount allowed by RTR's formal written policies and procedures.

Recommendation

RTR should amend its fiscal years 2005 and 2006 UFRs as necessary identify the these unallowable fringe benefit and bonus expenses as being nonreimbursable to the Commonwealth. If RTR does not have sufficient non-state funds to pay for these nonreimbursable expenses, DMR should take whatever measures it considers necessary, including recoupment of these funds, to resolve this matter. In the future, RTR should take measures to ensure that only allowable fringe benefit and bonus expenses are expensed to its state-funded programs.

Auditee's Response

In response to the audit result, RTR officials stated, in part:

> *We do not dispute the overall finding in this area . . . .*
>
> *Changes Made to Correct this Issue:*
>
> - *The Benefit Time Policy has been changed.*
> - *We will file an amended UFR if warranted.*

In addition, a representative from RTR's private accounting firm provided the following comments:

> *The SAO has identified four instances in which RTR's former President and former CEO provided additional fringe benefits beyond those offered to all employees, thereby resulting in costs that were not reimbursable under funding contracts, but which were not reported as such. Three of these instances cited employee efforts (hours worked) beyond what was required under the employees' normal responsibilities as the reasons for the additional compensation or time off. Although RTR's Employee Guidebook did not include specific provisions for these circumstances, there is no evidence that they were applied selectively, but rather on an as-needed basis with no indication that any employee who might be asked to work extra hours would be denied the ability to offset those hours with time off or compensation. As a result, it does not appear that the related cost should be considered additional fringe benefits since the employees were simply given time off (or in one case, $2,500 in compensation) in lieu of extra hours worked, a common and accepted workplace practice.*
>
> *The fourth instance involving the increase of the Executive Director's vacation time by 10 days per year above the policy limit was clearly a cost that should have been identified as non-reimbursable. RTR had ample sources of revenue to offset such costs and failure to report these costs as nonreimbursable is indicative of a failure of RTR's ability to properly identify all such costs.*
>
> *The SAO's recommendation that OSD should recover $26,299 from RTR relative to these costs is not consistent with OSD regulations. Rather, OSD should consider requiring RTR to file an amended UFR for the period in question, and reclassify the costs in question as nonreimbursable, but this would not give rise to a liability given RTR's available offsetting revenues.*

Auditor's Reply

We believe that the actions taken by RTR in this matter were necessary and responsive to our concerns in this area. However, we do not agree with the assertions made by the representative of RTR's private accounting firm that these benefits were not additional fringe benefits provided to these individuals. Rather, as noted above, since the additional benefits to these individuals were not provided in accordance with RTR's formal written policies and procedures, and because RTR's board had not granted either RTR's President or its Executive Director the authority to provide these additional benefits, these expenses clearly represent nonreimbursable expenses under RTR's state contracts.

4. INADEQUATE CONTROLS OVER PERSONNEL ACTIVITIES AND ADMINISTRATION

During our audit, we identified a number of areas in which RTR needed to improve its administration of its personnel activities. Specifically, although RTR had a policy that required all agency staff to complete individual time sheets documenting the number of hours worked by each staff person in each program, during our audit period at least 11 of RTR's administrative employees were not required to complete these time records in this manner. We also found that only one personnel file of these 11 staff members contained a formal job description indicating the employee's job-related responsibilities. Further, contrary to the terms and conditions of RTR's state contracts, there was no evidence that RTR's board ever formally evaluated the performance of its Executive Director. In fact, only one the 11 staff members in our sample (RTR's Vice-President of Finance) had any evidence of receiving a performance evaluation during the entire audit period. As a result, there is inadequate assurance that all of the salary-related compensation of these 11 employees, which totaled $3,032,646 during fiscal years 2005 through 2008, was properly allocated to RTR's state-funded contracts. Further, by not establishing formal job descriptions for these positions and not conducting regular performance evaluations, RTR lacked adequate controls over its administrate staff to establish appropriate accountability for their administrative activities or criteria against which these staff members could be evaluated.

OSD has promulgated Terms and Conditions for Human and Social Service Contracts (General Contract Conditions), with which all contracted human service providers such as RTR must comply. According to these General Contract Conditions, contracted human services providers are required to maintain accurate and complete financial records, including payroll records, in order to receive reimbursement of these costs. Specifically, these General Contract Conditions state, in part:

> *The provider will maintain personnel records for each employee. These records shall include, but not be limited to . . . payroll records, and . . . attendance records or effort reports, documentation program and assignment and hours and days worked.*

Further, 808 CMR 1.04 (1), promulgated by OSD, states:

> *The Contractor and its Subcontractors shall keep on file all data necessary to satisfy applicable reporting requirements of the Commonwealth (including DPS [now OSD], the Division of Health Care Finance and Policy and Departments), and financial books, supporting documents, statistical records, and all other records which reflect revenues associated with and costs incurred in or allocated to any Program of services rendered under the Contract. The Contractor and its Subcontractors shall maintain records of all types of expenses and income or other funds pertaining to the Program paid to the Contractor by every source, including from each Client. Books and records shall be maintained in accordance with generally accepted accounting principles as set forth by the American Institute of Certified Public Accountants (AICPA) . . . .*

Despite these requirements, we found that during our audit period at least 11 of RTR's administrative staff were not required to complete time records reflecting the hours worked or function benefited, as follows:

President
Vice-President Development/Acting CEO
Vice-President Legal Counsel
Vice-President Training/Development
Assistant Vice-President Quality
Workshop Coordinator
Executive Director
Vice-President Finance
Vice-President Residential
Assistant Vice-President Development
Administrative Coordinator

Instead, the attendance of these 11 employees was tracked on a "group" timesheet in which only employee names and the weekly total of hours they worked were filled out. Moreover, we found that the employees often did not sign these group timesheets, approved their own timesheet, and did not indicate the day or hours worked per day or the function benefited. The time and attendance process followed by these 11 employees is contrary to RTR's personnel policies and procedures, which require all staff to complete individual time sheets documenting the hours they worked and the location or program in which they worked. These policies and procedures also require timesheets to be signed by the employees and their supervisors.

Further, according to the General Contract Conditions, the Board of Directors of a human service organization such as RTR is required to fulfill certain oversight responsibilities, including the obligation to "annually review its executive director's or other more senior manager's performance and set that person's compensation by formal vote." However, our review of the Executive Director's personnel file, the personnel files of 10 other members of RTR's senior management staff, and the minutes from RTR Board of Directors meetings indicated that the board had not routinely conducted formal written performance evaluations on any of 11 staff members. In fact, only one staff member--RTR's Vice-President of Finance--had a performance evaluation in their personnel file.

During our audit, we brought this matter to the attention of RTR officials, who responded that, effective immediately, all time records and personnel evaluations in accordance with the terms and conditions of their state-funded contracts.

Recommendation

RTR should implement internal controls and OSD-compliant policies and procedures to ensure that it has adequate controls over its human resource administration. At a minimum, such controls should include detailed job descriptions in all personnel files, a formal evaluation process with at least annual evaluations for all staff, and the requirement that all staff to complete individual timesheets in compliance with state regulations.

Auditee's Response

In response to the audit result, RTR officials provided the following comments:

> *We do not dispute the overall finding in this area.*
>
> *Changes Made to Correct this Issue:*
>
> - *We have begun the process of putting Job Descriptions in place for all positions in the corporation. While this process is not complete, we expect that it will be by the end of January 2009. Once this process is completed, regular performance evaluations will be scheduled for all positions.*
> - *All employees are now being required to fill out time sheets.*
> - *Changes to the governance structure of the organization now makes it possible for the Board of Directors to enforce compliance in this area of the President/CEO.*

In addition, a representative from RTR's private accounting firm provided the following comments:

> *The SAO has identified 11 administrative employees who did not maintain daily timesheets in accordance with RTR's policy. These individuals consisted primarily of upper management. While SAO is correct that this is technically inconsistent with RTR's policy, correcting this condition could consist merely of exempting by policy specific positions from this type of time reporting when, as is the case with these individuals, they are more easily charged to functional categories through an allocation policy, an approach that is consistent with both generally accepted accounting principles and OSD regulation. The concerns raised by the SAO that this condition provides inadequate assurance that related salaries were charged to appropriate functions [is] unfounded. Annual tests of payroll postings indicate that RTR's system properly allocates these individuals to appropriate functions (all of the 11 work primarily in one function, and only 2 of the 11 work in program functions). Moreover, the process of preparing the UFR and calculating FTE data provides additional assurance with regard to proper reporting.*
>
> *The SAO also cited one instance in which a job description was omitted from 1 of the 11 files, and 10 instances in which performance evaluations were not documented in the files. These are valid concerns and controls should be implemented to ensure they are addressed.*

Auditor's Reply

We believe that the actions taken by RTR in this matter were necessary and responsive to our concerns in this area. However, we do not agree with the assertions made by the representative of RTR's private accounting firm regarding this issue. Based on our review of agency records, no documentation exists to substantiate the allocation for these administrative costs during the period of our audit were done properly. As noted in our report, the time and attendance records for these employees do not contain any information about the program or function in which these employees were working as required by OSD. Therefore, the allocation of these employees time cannot be substantiated by the documentation kept on file at RTR. Based on this, our concern about the accuracy of the allocation of these expenses is clearly well-founded. This concern is substantiated by the fact that, in its response to Audit Result No. 2, RTR states that its President spent some of his time conducting fundraising activities, yet none of this person's time was allocated to this activity in the UFRs RTR filed with OSD.

5. INEFFICIENT OPERATION OF TWO PROGRAMS RESULTING IN THE UNDERSTAFFING OF THESE PROGRAMS, AT LEAST $3,974,935 IN EXCESSIVE OVERTIME COSTS, AND THE ADDITIONAL COMMONWEALTH FUNDING TOTALING $80,749 TO COVER PROGRAM DEFICITS

We found that during our audit period, RTR provided full-time equivalent (FTE) staffing in two of its residential programs that was significantly lower (between 26% and 44%) than what was required by the state contracts that funded these programs. As a result of its not being able to provide the required FTE program staff, RTR had to pay overtime compensation that was between 218% and 812% above what was approved by DMR in the contracts that funded these two programs and also hire relief staff to provide the required level of services in these two programs. In one instance, these excessive overtime expenses resulted in DMR's having to agree to amend the contract that funded one of these two programs and provide RTR with an additional $80,749 to cover program deficits. Further, given that a significant amount of the program services in these two programs was provided by overtime and relief staff rather than through the required level of FTE staff, there is inadequate assurance that the quality of the services provided by RTR in these programs during our audit period was in compliance with RTR's contracts with DMR.

The Audit Resolution Policy for Human and Social Services, issued by OSD, states the following about the underutilization of program staffing:

> *This provision is intended to be utilized when there are indications that staffing may not have been provided as agreed upon in the original contract or amendment documents as needed to carry out the program of services. For purposes of this section, emphasis should be placed upon the review of staff credentials and full-time equivalents (FTEs) provided. Review of the cost of staffing shall take into consideration payroll, the cost of relief staff and consultants, compensated overtime performed by existing staff, related taxes, related benefits, and the like. For purposes of resolving audit findings concerning reimbursement, a determination that any program or cost category for staff related spending was below 90 percent of the funds budgeted or allocated for staffing in the relevant contract, shall be referred to the purchasing Department for review of actual service delivery and quality levels. Purchasing Departments are responsible for resolving the deficiency by determining if service delivery requirements, performance standards and/or minimum staffing or program standards have been met or need to be revised.*

During our audit, we performed a budget-to-actual analysis of program expenses for RTR's state-funded residential programs. Based on this review, we determined that RTR had significant staffing shortages ranging from 26% to 44% in these programs during our audit period, as follows:

Residential Programs Staff Shortages

Year	Program	Contract Budget FTEs	Contract Budget Amount	Actual Provided FTE	Actual Provided Amount	% Understaffed	Actual Staff Expense over Budgeted Amount
2005	Residential Plymouth Program	76	$1,915,648	46	$2,060,524	40%	$144,876
2006	Residential Plymouth Program	127	$2,946,011	72	$3,047,888	43%	$101,877
2005	Residential South Coast	163	$3,850,273	91	$4,038,927	44%	$188,654
2006	Residential South Coast	178	$4,183,273	131	$4,576,412	26%	$393,139
	Total	544	$12,895,205	340	$13,723,751	38%	$828,546

As shown above, RTR was significantly understaffed in both residential programs in both years reviewed, by an average of 38%, than what was contractually budgeted. However, despite the significantly lower number of FTEs provided in each program, each program's total staffing expenses were actually higher than budgeted, as shown in the above table, because RTR had to pay extensive overtime compensation to its staff and also hire relief staff in an attempt to make up for this shortfall in the contractually required full-time staffing for these programs. Consequently, RTR had significantly higher overtime costs than what was budgeted in these contracts, as shown in the table below:

Overtime and Relief Staff Expense

Year	Program	Contract Budget	Actual	Amount Excessive	Percentage
2005	Residential Plymouth Program	$283,905	$902,919	$619,014	218%
2006	Residential Plymouth Program	187,905	1,073,592	885,687	471%
2005	Residential South Coast	237,385	1,813,022	1,575,637	664%
2006	Residential South Coast	107,385	1,011,982	904,597	842%
	Total	$816,580	$4,801,515	$3,984,935	488%

Further, the additional staffing expenses resulting from significantly higher overtime and relief staff expenses led to program deficits in the Residential South Coast contract in fiscal year 2005. Consequently, DMR provided RTR with an additional $80,749 in Commonwealth funding by amending its Residential South Coast contract for the reason of providing one-time funding to cover program deficits. However, as detailed, the program would not have incurred such deficits had it complied with its contractual obligations and provided staffing at the budgeted levels.

RTR's inefficient management practices not only cost the Commonwealth additional funds, but, given the fact that a significant amount of the program services in these two programs was provided by overtime and relief staff rather than the required level of full-time staff, also calls into question whether the quality of the services provided by RTR in these programs during our audit period was in compliance with RTR's contracts with DMR.

Regarding this matter, RTR officials stated that they are aware of these staffing issues and have been working to increase the full-time staffing levels in these residential programs.

Recommendation

DMR should routinely review the staffing that RTR is providing in these two programs and determine whether it adequately meets the needs of the consumers in these programs. Based on these reviews, DMR should determine whether it wants to continue to fund these programs with this provider.

Auditee's Response

In response to the audit result, RTR officials provided the following comments:

> *We strongly disagree with this finding. First and foremost, staffing problems is an industry-wide issue of such gravity that a study entitled "The Future of the Human*
>
> *Services Workforce In Massachusetts" (conducted by the Donahue Institute at UMASS-Amherst and commissioned by the MA Council of Human Service Providers) found that the growth of jobs in this area (human services) coupled with low wages and a relatively small pool of possible applicants has created a statewide crisis in this area that is most paramount in residential service providers due to the need for 24-hr. staffing in many programs. RTR has been at the forefront of efforts to try to minimize this chronic problem by having an aggressive international recruitment program (using H1 and J1 visas) and we actively recruit using all available tools (newspapers, Internet sites, Job Fairs, College outreach, Career Centers). The fact of the matter is that the statements made about RTR could be made about any residential provider in the Commonwealth. As such, it should be removed. Furthermore, it is important to note that relief and overtime expenses are reported on the same line of the UFR making it impossible to differentiate what amounts were overtime put in by regular program staff versus the use of relief staff.* ***In ALL instances, RTR has always maintained contractually required staffing patterns.***

The "Additional Commonwealth Funding Totaling $80,749" represents one-time monies amended into our contract to cover extraordinary costs associated with having to provide 24 hr/day staffing for a medically compromised, behaviorally intense, deaf consumer while that individual was in the hospital. If we had not done so the individual would not have been able to receive the medical treatment needed. Once again, this is an increasingly common issue that has become more prevalent in recent years as the population has aged and hospital resources have become more stretched creating a situation whereby hospitals are refusing to take in individuals with significant mental health, behavioral or sensory needs (e.g. Deaf) unless programs provide 1:1 staffing.

How We are Approaching this Issue:

- *RTR continues to use all tools available for staff recruitment from International recruiting programs to online and other tools.*
- *We are actively working with medical providers and hospitals to educate them about our consumer populations to hopefully decrease their hesitance in serving our consumers.*

In addition, a representative from RTR's private accounting firm provided the following comments:

The SAO has identified lack of adequate full-time staffing levels as a source of inefficiency since this leads to the need to pay higher pay rates in the form of overtime, shift differential and relief pay. While this may be true, criticism on this point is largely inappropriate given that this is primarily a function of economic realities in the employment market during the period under audit. In fact, RTR has been a pioneer in this area, being among the first to introduce a foreign staff work visa program to help reduce the negative impact of a strong employment market during the period in question.

The SAO also cited a failure to provide adequate staffing by virtue of comparing full time equivalent (FTE) data in the service contracts to that of the UFR. This analysis is flawed, however, in that the UFR includes no FTE data for the hours compensated as relief pay, whereas the service contracts do assign FTE data to relief pay. The result is that the percentages of understaffing cited by the SOA are overstated.

Auditor's Reply

We do not dispute the fact that, during our audit period, RTR took measures to try to ensure that appropriate staffing levels were being maintained in the two programs in question. However, we cannot comment on RTR's assertion that it always maintained its contractually required staffing patterns. This is because, although RTR did attempt to maintain the requisite number of staff in these programs, we could not determine whether the qualifications of the individuals being utilized by RTR in these programs on a relief or overtime basis was consistent with the qualifications of the full-time staff that should have been employed in these positions as required by RTR's contracts with DMR. Further, we do not dispute the fact that there may be some issues with being able to hire and retain properly trained program staff. However, RTR has the ability to address these staffing issues through its budget negotiations and contracting process with DMR. If RTR believed that it could not staff the program at the required FTE levels, it should have raised this concern with DMR in the contracting process and discussed the possibility of either discontinuing these contracts or modifying the contracts (e.g., reducing services or requesting additional funding for program staff) to the point where it could have provided the contractually agreed-upon staffing levels. Although it may be true that many human service providers across the Commonwealth may be facing a short supply of qualified direct care program staff, RTR entered into contracts with DMR that indicated that it had the ability to provide the required program staffing, which it should not have done if it had full knowledge, as it suggests in its response, that it was not going to be able to provide this staffing. Such contracting practices result in operational inefficiencies and could result in a reduction in the quality of program services. Furthermore, although RTR claimed in its response that the additional Commonwealth funding totaling $80,749 represented a one-time expenditure for a specific consumer, the actual contract amendment stated that the additional funding was to cover program deficits. If the purpose of the funding was to cover costs for a specific consumer, it should have stated such in the amendment. Nevertheless, based on its response, RTR is taking measure to try to address our concerns in this area.

Contrary to the assertions made by the representative of RTR's accounting firm, our audit analysis was not in any way flawed. In fact, as noted in our report, our analysis was based on information from RTR's records, contracts, and audited financial statements. Our report accurately reports the variance in both the FTEs provided by RTR in these programs as well as the variance in the dollar values of the overtime and relief staff expenses in these programs. The purpose of our analysis was not to conclude that the programs in question were understaffed, which could not be determined since RTR's records did not facilitate the ability to readily translate relief and overtime expenses into FTEs. Rather, the purpose of presenting this information was to demonstrate that, although RTR had continually entered into contracts with DMR to operate these programs at certain FTE staffing levels, RTR was not able to meet these contractual requirements with full-time staff and was routinely required to staff these programs with overtime and relief staff, thereby incurring excessive costs in these areas.

6. QUESTIONABLE ALLOCATION OF $141,478 IN NONREIMBURSABLE EXPENSES

During fiscal year 2007, RTR allocated all of its reported nonreimbursable administrative expenses, which totaled $141,478, to only one of its federally funded programs rather than allocating these costs to all of its programs using an acceptable cost allocation plan as required by OSD regulations. This questionable allocation resulted in RTR's being able to expense the entire $141,478 in administrative nonreimbursable expenses, of which $101,997 otherwise would have been subject to recoupment by the Commonwealth had they been properly allocated to RTR's state-funded programs.

In providing program services, agencies such as RTR incur both direct costs, which can be attributable to a specific program or activity, and indirect costs, which are more general in nature and cannot be associated with one specific program or activity. Because indirect costs cannot be attributable to a specific program or activity, they need to be allocated to each of an agency's activities using a cost allocation plan. OSD has established regulations for the allocation of indirect expenses against state contracts. According to 808 CMR 1.02, promulgated by OSD, contracted human service providers are required to maintain a written cost allocation plan for indirect administrative expenses, as follows:

> *Administration and Support Costs (management and general) include expenditures for the overall direction of the organization, general record keeping, business management, budgeting, general board activities, general legal expenses and related purposes. "Overall direction" includes the salaries and expenses of the chief officer of the organization and the chief officer's staff. If such staff spends a portion of its time directly supervising fundraising or Program service activities, such salaries and expenses are considered indirect fundraising or Program costs and should be prorated (allocated) among those functions by position title or type of expense. Allocation of program support expenses…must be made using a written cost allocation plan in accordance with GAAP as described in the sections covering Administrative Costs and Costs Which pertain To Certain Functions . . . . Allocation of Administrative expenses that pertain to the "Overall Direction" of the organization to programs…must also be made by utilizing a written costs allocation plan using the same principles as noted above or as described in the Direct Method for allocating indirect costs to federal programs of OMB [Office of Management and Budget] Circular A-122.*

OSD's 2007 UFR Compliance Supplement gives guidance on how human service contractors such as RTR should account for any expenses that are nonreimbursable under state contracts including indirect administrative costs, by stating, in part:

> *All costs, whether reimbursable or non-reimbursable, associated with programs or supporting services (administration, fundraising, and non-program (non-charitable)*

> *activities are supporting services) should be classified and reported in the program or supporting service that they relate to.*
>
> *Reimbursable and non-reimbursable costs should be categorized and allocated to, the programs or supporting service (such as non program and fund-raising) that they were incurred in, irrespective of any other source of funds that may be available in other programs or supporting service to defray these costs.*
>
> *Often, non-reimbursable costs are inappropriately reported in a separate cost category or program when a provider does not have an adequate level of non-public funds available in the program, or in other programs, or in supporting services, to defray the non-reimbursable costs. Contributing to this issue is the requirement that the fund balance of the Surplus revenue retention fund pool may not be used to defray non-reimbursable costs because the balance in this account was derived from public funds.*

During fiscal year 2007, RTR reported in the UFR that it filed with OSD that it incurred the following nonreimbursable administrative expenses:

2007 UFR Reported Administrative Non-Reimbursable

Description	Amount
Total President's Salary	$79,180
Executive Director Salary, Exceeding OSD Limits	11,572
Acting CEO Salary, Exceeding OSD Limits	23,805
Miscellaneous	22,473
Bad Debt	892
Penalties	1,181
Depreciation of Donated Assets	2,375
Total	$141,478

During our audit, we determined that, contrary to OSD guidelines, RTR did not have a written cost allocation plan for its indirect costs. However, although RTR did not have a formal cost allocation plan, we did note that, for the majority of its indirect expenses, RTR was utilizing an indirect cost allocation method that was an acceptable method to OSD. Despite this, during fiscal year 2007, rather than allocating its nonreimbursable expenses using this same method, RTR allocated all of the $141,478 in nonreimbursable expenses that it reported it incurred during this fiscal year to its Day Habilitation program, which is funded by Medicaid.

During the prior two fiscal years (2005 and 2006), RTR did not allocate its administrative nonreimbursable expenses to any programs. Rather, during these two fiscal years, RTR had enough eligible non-state revenue to offset their administrative nonreimbursable expenses and therefore, these expenses were not allocated RTR to its programs but rather were reported as separate expenses and offset by non-state revenue in its UFRs. However, in fiscal year 2007, RTR did not have sufficient eligible non-state administrative revenues to offset the $141,478 in administrative nonreimbursable expenses reported in this fiscal year, as shown in the following table:

UFR Reported Administrative Non-Reimbursable Expense Detail

	2005	2006	2007
Admin. Nonreimbursable Expense	$66,322	$205,550	$141,478
Allocation of Nonreimbursable Expense	0	0	($141,478)
Admin. Nonreimbursable Expenses after Allocation	$66,322	$205,550	0
Eligible Admin. Nonreimbursable Revenue Offset	95,561	651,128	$39,481
Excess of Nonreimbursable Offsets over Expenses	$29,239	$445,578	($101,997)

Consequently, RTR elected to allocate all of its nonreimbursable expenses to its federally funded Day Habilitation program, which effectively mitigated its having to identify any non-state sources of revenue to pay for these expenses.

Regarding nonreimbursable expenses, OSD's UFR reporting instructions state the following:

> *Any Excess of Non-Reimbursable Expenses over Eligible Revenue Offsets is subject to recoupment where the program is purchased by the Commonwealth and must be recognized as a liability on the Financial Statements*

Since the Commonwealth did not purchase services in RTR's Day Habilitation program, the excess of nonreimbursable expenses for which there is no offsetting revenue in this program is not subject to recoupment by the state. However, we determined that if RTR had allocated its nonreimbursable expenses during this fiscal year in the same manner that it had allocated all of its other nonreimbursable administrative expenses, and in a manner consistent with OSD guidelines, it would have had to reimburse the Commonwealth $101,997.

Regarding this matter, RTR officials stated that they had discussed allocating all of RTR's nonreimbursable expenses to the Day Habilitation program with its private accounting firm and that a representative from this firm told them that this was an acceptable allocation. Further, these officials stated that RTR's board signed RTR's fiscal year 2007 UFR and in so doing authorized the method used to allocate the nonreimbursable expenses in question. However, contrary to these assertions made by RTR officials, OSD regulations clearly indicate that an expense should be recognized in the program it incurred in and that, if it is an indirect expense that must be allocated, there must be a formal written allocation method. In this instance, RTR neither reported these expenses in the program or supporting service that they relate to nor had a written allocation plan that allowed for these expenses to be allocated in such a manner.

Recommendation

RTR should amend its fiscal year 2007 UFR and properly allocate all nonreimbursable expenses to the function/program that they were incurred or have a written allocation plan that justifies the allocation. If RTR does not have enough eligible revenue to cover its nonreimbursable expenses, DMR, in conjunction with OSD, should seek recoupment of the state funds that RTR used to pay for these nonreimbursable expenses.

Auditee's Response

In response to the audit result, RTR officials stated, in part:

> *We disagree with this finding. Our UFR is reviewed by our independent auditor. Our allocations are consistent with the guidelines included in the UFR Preparation Manual, as confirmed and verified by the review response of our independent auditors . . .*

In addition, a representative from RTR's private accounting firm provided the following comments:

> *The SAO has suggested that fiscal year 2007 nonreimbursable administrative expenses should be allocated to all programs using an acceptable cost allocation plan as required by OSD regulations, citing 808 CMR 1.02 which requires the use of cost allocation plans to properly allocate functional costs in accordance with GAAP. UFR lines 52e and 55e, the lines used to allocate total administrative expense and administrative costs are not subject to this guidance, however, since the very notion of allocating a cost incurred in one function to another is inconsistent with GAAP. That is why these lines do not affect the functional totals automatically accumulated in the UFR and summarized on the UFR's Statement of Functional Expenses. Those totals are consistent with GAAP-prepared financial statements and are considered as such and covered by the Auditor's opinion that accompanies the UFR, whereas schedules A and B, which contain the allocation in question, are not audited schedules and are not covered by the Auditor's opinion as they do not conform to GAAP.*
>
> *The SAO has suggested that properly allocating the administrative nonreimbursable costs would result in a required reimbursement to the Commonwealth in the amount of*

$101,997. The SAO fails to recognize that all available offsetting revenue is available to defray nonreimbursable costs, regardless of which functions or programs the costs were incurred in and which generated the available revenue offsets. In fact, the 2007 UFR reflects available offsetting revenues that exceed total nonreimbursable costs by the sum of $907,183. Moreover, the SAO fails to recognize that RTR had accumulated unrestricted earnings of $1,330,501 as of June 30, 2007, net of a surplus revenue retention pool deficit (attributed to Commonwealth funding) of ($4,034,442) which means RTR had approximately $5,364,943 of total available offsets to nonreimbursable costs. Under these circumstances, it is inconceivable that any portion of the 2007 nonreimbursable costs would be subject to recoupment by the Commonwealth.

As of the date of this report, the 2007 UFR has been subjected to the OSD desk review process. While OSD requested certain additional information be filed to provide greater detail, the method of reporting nonreimbursable costs and offsets was not challenged in any way.

Auditor's Reply

We do not agree with the assertion made by the representative of RTR's private accounting firm that the allocation of the nonreimbursable administrative expenses in question was done in a proper manner. As noted in our report, contrary to OSD guidelines, RTR did not have a written cost allocation plan for its indirect costs. However, although RTR did not have a formal cost allocation plan, we did note that for the majority of its indirect expenses, RTR was utilizing an indirect cost allocation method that was an acceptable method to OSD. Despite this, during fiscal year 2007, rather than allocating its nonreimbursable expenses using this same method, RTR allocated all of the $141,478 in nonreimbursable expenses that it reported it incurred during this fiscal year to its Day Habilitation program funded by Medicaid. In his comments, the representative from RTR's private accounting firm asserts that the allocation of these general administrative expenses to this one program was proper. However, this method of allocation is clearly inconsistent with OSD requirements. Contrary to the representative's claim, these costs were not associated with a specific function but were general in nature and thus subject to OSD cost allocation requirements. This is evidenced by the fact that only the nonreimbursable portions of these expenses were allocated to this one program. For example, RTR allocated what it determined to be the reimbursable portion of the President's salary to different programs during this fiscal year using the same allocation formula that RTR used to allocate all of its reimbursable indirect administrative costs. However, RTR arbitrarily charged the total amount of the nonreimbursable portion of this salary expense directly to this one program, which is an inconsistent treatment to these expenses. Further, as noted above, RTR allocated all of its other administrative costs this year using this formula and more significantly, it was the only year during our audit period when RTR allocated all of its nonreimbursable costs to one program rather than using an allocation formula. Clearly, since none of these nonreimbursable administrative expenses represented a direct cost that could be attributable to RTR's Day Habilitation program, the proper accounting treatment for these expenses would be to allocate them across all programs using an acceptable cost allocation formula and not to expense them directly to this one program.

Additionally, the assertion made by the representative of RTR's private accounting firm that "all available offsetting revenue is available to defray nonreimbursable costs, regardless of which function or programs the costs were incurred in and which generated the available revenue offsets" is incorrect. OSD's 2007 UFR Compliance Supplements, page 22, states the following:

> *Contractor organizations are required to disclose the existence and value of all anticipated non-reimbursable costs, as identified in 808 CMR 1.05 (1) - (28), and identify the offsetting revenue used to defray the non-reimbursable costs in program budgets of contracts with purchasing agencies of the Commonwealth. All incurred non-reimbursable costs and their value must be reported in Supplemental Schedule B_PSI expenses of the Uniform Financial Statements and Independent Auditors Report (UFR) as either a state or federal non-reimbursable cost.*

Finally, contrary to what the representative states, OSD regulation 808 CMR 1.03(7) specifically prohibits contracted human service providers from using any surplus revenues they realize under their state contracts to pay for nonreimbursable expenses by stating, "provided that no portion of the surplus may be used for any non-reimbursable cost set forth in 808 CMR 1.05."

OTHER MATTERS

During the course of our audit, we identified one other issue, which although did not involve instances of noncompliance to specific laws, regulations, policies, procedures, or contractual terms and conditions as the ones detailed in the Audit Results section of this report, did have an impact on the financial viability of RTR. Consequently, we are disclosing this issue to RTR's management for its consideration.

THE OPERATION OF RTR'S VENTURE PROGRAM AND FUNDRAISING ACTIVITIES IS ADVERSELY AFFECTING THE OVERALL FINANCIAL VIABILITY OF RTR

Sound business practices advocate that entities such as RTR evaluate their performance and take the measures necessary to ensure that the entity operates in the most efficient and effective manner. However, we found that during our audit period, RTR conducted two activities from which it derived significant financial losses and did not appear to make any changes in these activities to improve their efficiency. First, RTR's Venture Program is a community services program that provides various services to RTR's consumers and the community. During our audit period, the Venture Program included recreation programs, three bookstores (located in Marshfield, Plymouth, and Falmouth), a farm located in New Hampshire, an Internet sales activity, an ice cream shop, a consignment shop, two hotels (the Ocean Village Motel and the Kingston Inn), and an entity involved in consulting called Inquintessence that was not providing any services during our audit period. The Venture Program does not receive any direct state funding.

During the period covered by our audit, we determined that the Venture Program incurred significant losses, as detailed in the table below:

Venture Program Operating Results

	2005	2006	2007	Total
Total Revenue	$656,995	$581,476	$658,228	$1,896,699
Total Expense	1,320,954	1,336,928	1,234,346	3,892,228
Operating Results	$(663,959)	$(755,452)	$(576,118)	$(1,995,529)

The losses in this program affected RTR's overall financial viability. Specifically, these losses had to be funded/offset by profits obtained in RTR's other state- and federally funded programs, which were insufficient to offset the losses in the Venture Program during the audit period, as detailed below:

RTR Operating Results from Programs

Operating Results	2005	2006	2007	Total
State-Funded Programs	$7,292	$(229,299)	$309,020	$87,013
Day Habilitation Program (Medicaid)	627,008	556,983	235,576	1,419,567
Venture Program	(663,959)	(755,452)	(576,118)	(1,995,529)
Total, All Programs	$(29,659)	$(427,768)	$(31,522)	$(488,949)

RTR does have other fundraising revenue but in most years during our audit period, the expenses associated with these revenues exceed the revenues collected. The results of RTR's total operating results for all departments, including its fundraising activities, during our audit period is as follows:

RTR Total Organization Operating Results

Department	2005	2006	2007	Total
Total, All Programs	$(29,659)	$(427,768)	$(31,522)	$(488,949)
Administration	29,239	445,578	39,481	514,298
Fundraising	(129,808)	104,419	(100,514)	(125,903)
Total Organization	$(130,228)	$122,229	$(92,555)	$(100,554)

As shown in the table above, the reason for the net losses in both fiscal year 2005 and 2007 was primarily due to the operating losses incurred in RTR's Venture Program and deficiencies in its fundraising activities. Further, the only reason RTR did not incur a significant loss in 2006 was because it sold several of its properties, which resulted in an increase in administrative revenue of $506,893.

In our opinion, RTR's management should reevaluate the need to operate its Venture Program and should conduct its fundraising activates as designed. The operation of these activities in this manner clearly has a negative financial impact not only on the operation of RTR's other programs but also on the financial viability of the organization as a whole. Further, we believe that any profits realized in RTR's state-funded programs would best be used to yield better program performance and effectiveness within these programs rather than subsidizing RTR's other unprofitable activities.

During our audit, we brought this matter to the attention of RTR's current Executive Director, who agreed with our assessment. Further, at RTR's October 30, 2007 Board of Directors meeting, the Executive Director made the following disclosures to the board:

> *I have reviewed the RTR UFRs for the past seven years (FY2001 through FY2007) and have prepared the attached worksheet that details the analysis. The following findings and deductions are intended to summarize the analysis.*
>
> *For the period FY2001 through FY2007:*
>
> *Gains on RTR's DMR/ State Programs and the sale of assets funded by DMR accounted for $4.1 million, or 100% of all gains from RTR operations (e.g. those programs in aggregate, showed a significant surplus every year).*
>
> *RTR "ventures" accounted for $3.5 million, or 100% of all losses from RTR operations.*
>
> *Sale of properties were necessary in FY'2003 and FY'2006 in order to replace depleted working capital associated with the aforementioned losses.*
>
> *RTR's Line of Credit was converted to a Term note for $541,000 in FY'2003 to cover losses associated with the "ventures."*
>
> *The losses attributable to the "ventures" have escalated each year, from 200,000 to 577,000, to 755,000 in FY2001, 2004, and 2006 respectively.*
>
> *The funds to offset the losses attributable to the "ventures" could only have come from DMR/state funded programs, increased debt, or sale of properties funded by DMR/ state contracts.*
>
> *RTR has directed a disproportionate amount of its management focus and has leveraged its program related assets to purchase non-performing, over-valued "venture" associated properties.*
>
> *The magnitude and persistence of the losses reveal a structural imbalance that the agency has been reluctant and/or slow to identify and unable to correct.*