



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

Making government work better

OFFICIAL AUDIT REPORT-ISSUED NOVEMBER 19, 2012

The Institute for Developmental Disabilities, Inc.

For the period July 1, 2009 through June 30, 2011



TABLE OF CONTENTS

INTRODUCTION AND SUMMARY OF FINDINGS AND RECOMMENDATIONS	1
OVERVIEW OF AUDITED AGENCY	3
AUDIT SCOPE, OBJECTIVES, AND METHODOLOGY	4
AUDIT FINDINGS	6
1. QUESTIONABLE RELATED-PARTY TRANSACTIONS TOTALING \$359,573	6
2. UNALLOWABLE CONTRACT BILLINGS TOTALING \$90,922	9
3. UNALLOWABLE FRINGE BENEFITS TOTALING \$23,839	11
a. Unallowable Vehicle Expenses Totaling \$11,739	11
b. Unallowable Employee Loans Totaling \$12,100	12
4. UNALLOWABLE PROGRAM EXPENSES TOTALING \$13,200 CHARGED TO STATE-FUNDED CONTRACTS	14
5. UNNECESSARY EMPLOYEE COMPENSATION TOTALING \$38,792 CHARGED TO STATE-FUNDED CONTRACTS	16
6. INAPPROPRIATE ALLOCATION OF \$9,335 IN FUNDRAISING EXPENSES TO STATE-FUNDED CONTRACTS	20
APPENDIX	22
PROGRAMS OPERATED BY IDDI	22

INTRODUCTION AND SUMMARY OF FINDINGS AND RECOMMENDATIONS

The Institute for Developmental Disabilities, Inc. (IDDI) was incorporated on July 1, 1982 under the provisions of Chapter 180 of the Massachusetts General Laws as a not-for-profit corporation. During our audit period, IDDI was providing approximately 110 severely to profoundly disabled children and adults with specialized educational, therapeutic, and residential services. On May 5, 2011, IDDI changed its name to Crystal Springs Inc.

Highlight of Audit Findings

- Contrary to state regulations, IDDI did not use a competitive bidding process to procure all of the \$359,573 in equipment and services it purchased from a related-party organization and did not enter into formal written agreements for these purchases.
- IDDI used Limited Use Rate Service Agreement (LUSA) funds totaling \$90,922 to purchase additional equipment and improve its facilities, rather than for their intended purpose, which is to provide unanticipated, intermittent, and as-needed services for developmentally disabled individuals.
- IDDI provided unallowable fringe benefits totaling \$23,839, which represents \$11,739 in unallowable vehicle expenses and \$12,100 in loans to several employees. These benefits were unallowable because IDDI had not established formal written policies and procedures to provide them to all employees.
- IDDI did not identify in its financial records rental income totaling \$13,200 that it received from its former Executive Director as revenue for its Adult Residential Program, or use this income to offset the state's cost of operating this program. Rather, IDDI reported this income in its fiscal year 2009 and 2010 financial statements as "other revenue" and used these funds to offset nonreimbursable expenses it had charged against its state-funded contracts.
- IDDI charged \$38,792 in compensation for one of its employees against its state contracts that was unnecessary and therefore unallowable under its state contracts.
- IDDI charged unallowable fundraising costs totaling \$9,335 against its state contracts.

Recommendations of the State Auditor

- IDDI should comply with Operational Services Division (OSD) regulations relative to the procurement of goods and services to ensure that it obtains the highest-quality services for the lowest possible price and should enter into formal written contracts with all of its contractors to both monitor their performance and protect itself from any legal issues that could arise.

- IDDI should consult with OSD and the Department of Developmental Services (DDS) to resolve the unallowable purchases it made using LUSA funds and ensure that any future LUSA funding it receives is expended in accordance with the LUSA guidelines established by DDS.
- IDDI should ensure that it does not use state funds to provide loans to staff members. Further, IDDI should remit to the Commonwealth the \$11,739 in unallowable vehicle expenses we identified and ensure that, in the future, it does not charge any unallowable vehicle expenses against its state contracts.
- IDDI should accurately report all program income in accordance with state regulations. Further, it should remit to the Commonwealth the \$13,200 it inappropriately charged to its state contracts by failing to report rental income from its former Executive Director as revenue to offset program expenses in its Adult Residential Program.
- IDDI should remit to the Commonwealth the \$38,792 in unnecessary compensation it inappropriately provided to one employee and ensure that it does not charge any such expenses against its state contracts in the future.
- IDDI should remit the \$9,335 in unallowable fundraising expenses it charged to its state contracts and ensure that any future fundraising expenses are properly identified and reported.

OVERVIEW OF AUDITED AGENCY

The Institute for Developmental Disabilities, Inc. (IDDI), located in Assonet, Massachusetts, was incorporated on July 1, 1982 under the provisions of Chapter 180 of the Massachusetts General Laws as a not-for-profit corporation. On May 5, 2011, IDDI changed its name to Crystal Springs, Inc. During our audit period, IDDI was providing approximately 110 severely to profoundly disabled children and adults with specialized education and therapeutic and residential services. (A detailed description of the services provided by IDDI appears in the Appendix to this report.)

During fiscal years 2010 and 2011, IDDI received revenue from a variety of sources, as indicated in the following table:

Summary of Revenue*

<u>Revenue Source</u>	<u>Fiscal Year 2010</u>	<u>Fiscal Year 2011</u>
Contributions and Gifts	\$ 76,273	\$ 65,750
Government In-Kind/Capital Budget	150,922	0
Other Grants	79,501	85,713
Department of Developmental Services	6,670,302	7,008,966
Department of Children and Families	1,042,857	786,994
MA Commission for the Blind	377,084	376,281
MA State Agency Non-POS	69,222	68,248
MA Local Government/Quasi-Government Entities	8,079,927	7,838,214
Non-MA State/Local Government	4,195,248	4,328,080
Direct Federal Grants/Contracts	105,844	104,719
Medicaid – Direct Payments	1,288,861	1,333,288
Client Resources	469,860	486,734
Investment Revenue	512,575	505,933
Other Revenue	353,495	643,846
Released Net Assets – Program	0	2,146
Released Net Assets – Equipment	<u>21,326</u>	<u>4,500</u>
Total Revenues	<u>\$23,493,297</u>	<u>\$23,639,412</u>

*This information was extracted from the Uniform Financial Statements and Independent Auditor's Reports (UFRs) that IDDI filed with the Commonwealth.

AUDIT SCOPE, OBJECTIVES, AND METHODOLOGY

The scope of our audit was to examine various administrative and operational activities of the Institute for Developmental Disabilities, Inc. (IDDI) during the audit period July 1, 2009 through June 30, 2011; however, in some instances it was necessary for us to extend the period covered by our audit in order to adequately examine certain transactions that were selected for testing during our review. 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 procedures consisted of the following:

1. A determination of whether IDDI had implemented effective management controls over certain activities, including contract administration, payroll and fringe benefits, corporate credit cards, related-party transactions, agency-assigned vehicles, separation agreements, and fundraising activities. These controls included:
 - Processes for planning, organizing, directing, and controlling program operations;
 - Policies and procedures to ensure that resource use is consistent with laws, rules, and regulations;
 - Policies and procedures to ensure that resources are safeguarded and efficiently used.
2. An assessment of IDDI'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. This assessment involved conducting transaction testing using judgmental sampling in the specified areas.

In order to achieve our objectives, we first assessed the internal controls established and implemented by IDDI over certain aspects of 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 IDDI's accounting system. We used this assessment in planning and performing our audit tests. We then held discussions with IDDI officials and reviewed organization charts and internal policies and procedures, as well as all applicable laws, rules, and regulations. We also examined IDDI's financial statements, cost reports, invoices, and other pertinent financial records and conducted transaction testing in the identified areas to determine whether the expenses

IDDI incurred during the period covered by our audit were reasonable; allowable; properly authorized and recorded; and in compliance with applicable laws, rules, and regulations. A detailed description of our transaction testing appears in the Audit Findings section of this report.

Our audit was not conducted for the purpose of expressing an opinion on IDDI's financial statements. We also did not assess the quality and appropriateness of program services provided by IDDI under its state-funded contracts. Rather, our audit provides findings and conclusions on the extent of IDDI's compliance with applicable laws, regulations, and contractual agreements, and identifies operational and administrative processes, methods, and internal controls that could be made more efficient and effective.

AUDIT FINDINGS

1. QUESTIONABLE RELATED-PARTY TRANSACTIONS TOTALING \$359,573

During fiscal years 2009 through 2011, the Institute for Developmental Disabilities, Inc. (IDDI) procured \$359,573 in heating, ventilation, and air-conditioning (HVAC) equipment and services from a related party, Thermo Mechanical Systems Corporation (Thermo Mechanical), of which the Chief Executive Officer and a member of the Board of Directors also served on IDDI's Board of Directors. Although IDDI disclosed Thermo Mechanical as a related-party organization in its financial statements, we found a number of problems with these transactions. First, contrary to state regulations, IDDI did not use a competitive bidding process to procure all of these services. As a result, IDDI cannot ensure that it obtained the highest-quality services for the lowest price. Second, IDDI did not enter into formal written agreements for any of these services. As a result, IDDI lacked a mechanism to monitor this contractor's performance and to protect itself from any legal issues (e.g., claims for nonperformance of services, liability claims for any property damage or personal injury) that could arise.

The Operational Services Division (OSD), the state agency responsible for regulating and overseeing the activities of all contracted human service providers such as IDDI, has promulgated 808 Code of Massachusetts Regulations (CMR) 1.02, which defines a related party as follows:

Related Party: Any person or organization satisfying the criteria for a Related Party published by the Financial Accounting Standards Board in Statement of Financial Accounting Standards No. 57 (FASB 57).

OSD's Uniform Financial Statements and Independent Auditor's Report (UFR) Audit & Preparation Manual provides the following FASB 57 definition for a related party:

Affiliates of the enterprise; entities for which investments are accounted for by the equity method by the enterprise; . . . its management; . . . and other parties with which the enterprise may deal if one party controls or can significantly influence the management or operating policies of the other to an extent that one of the transacting parties might be prevented from fully pursuing its own separate interests.

Although IDDI appropriately disclosed these related-party transactions in the financial statements it filed with OSD as required by OSD's regulations, we identified two other significant problems based on our review of IDDI's relevant documentation.

First, 808 CMR 1.03 (8), promulgated by OSD, establishes the following competitive procurement requirements with which all contracted human service providers such as IDDI must comply:

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 in 94 instances during fiscal years 2009 through 2011, IDDI procured equipment and services from Thermo Mechanical without using a competitive procurement process. The cost of these items and services totaled \$359,573. For example, on April 15, 2010, Thermo Mechanical provided construction work at an IDDI adult residence program located in Somerset at a cost of \$35,500, and on August 26, 2010, it completed a paving project at IDDI's school at a cost of \$69,720. Because these services were not competitively procured, IDDI cannot ensure that it obtained the highest-quality services for the lowest price.

Our audit also disclosed that IDDI did not execute any formal written agreements with this company for the equipment and services it purchased. As a result, IDDI lacked a mechanism to monitor this contractor's performance and to protect itself from any legal issues (e.g., claims for nonperformance of services, liability claims for any property damage or personal injury) that could arise.

During our audit, we brought this matter to the attention of the IDDI's Acting Executive Director, who stated that he planned to implement a new procurement policy that will require competitive bidding for all purchases of over \$2,500.

Recommendation

IDDI should comply with OSD regulations relative to the competitive procurement of goods and services and ensure that it enters into formal written contracts with all of its contractors.

Auditee's Response

In response to this issue, IDDI's Chief Executive Officer stated, in part:

The Organization's accounting manual that was provided to the State Auditor representative notes the following regarding procurement: "Purchase of goods and

services are conducted in a manner to provide, to the extent practical, open and free competition. This process will include to the extent practical solicitation of bids and proposals.” . . . The Organization did bid certain major projects with Thermo Mechanical Systems Corporation (Thermo Mechanical). The bids received provide competent evidence that Thermo Mechanical’s prices are competitive. This fact, coupled with the excellent results the Organization has experienced with the quality of Thermo Mechanical’s workmanship (i.e. no problems and exceptional, immediate service) for significant projects impacting the safety and security of the Organization’s clients, strongly indicates the Organization acted with prudence and care in selecting Thermo Mechanical to perform these projects.

The Organization has reviewed its records in detail pertaining to the transactions with Thermo Mechanical and notes the following factors that we would request you consider in relation to the total amount of questionable related party transactions, as 93% of the \$359,573 was either bid, below \$2,500 or not bid due to the nature of the work being related to emergency services (for which a bid process was not practical)

Auditor’s Reply

Despite what is stated in IDDI’s accounting manual, as noted above, during fiscal years 2009 through 2011, IDDI procured \$359,573 in HVAC equipment and services from a related party. Contrary to state regulations, it did not use a competitive bidding process to procure all of these services, nor did it enter into formal written agreements for any of these services. Controls such as competitive procurement procedures and formal written agreements, particularly when related-party organizations are involved, are essential in ensuring the integrity of the procurement and contract administration process.

In its response, IDDI states that it obtained competitive bids for some of the contracts in question. In fact, in two instances IDDI did obtain one other quote for services. However, this hardly constitutes a competitive bid process, and we do not agree that it provides sufficient evidence that Thermo Mechanical’s prices are competitive. Further, we see no reason why IDDI could not competitively award contracts for emergency repairs and services to be provided on an as-needed basis. Finally, in its response, IDDI suggests that it would not have utilized competitive procurement procedures for any services under \$2,500. However, as noted in its response, IDDI’s own policies and procedures do not establish a dollar limit under which competitive procurement is not necessary but rather state, “Purchase of goods and services are conducted in a manner to provide, to the extent practical, open and free competition. This process will include to the extent practical solicitation of bids and proposals.” We therefore again recommend that IDDI fully comply with OSD regulations relative to the competitive

procurement of goods and services and ensure that it enters into formal written contracts with all of its contractors.

2. UNALLOWABLE CONTRACT BILLINGS TOTALING \$90,922

During fiscal year 2010, IDDI entered into Limited Use Rate Service Agreements (LUSAs) with the Department of Developmental Services (DDS). According to DDS's policies, the funding provided under these contracts is to be used by contracted service providers such as IDDI to purchase unanticipated, intermittent, and as-needed services for developmentally disabled individuals. However, rather than using LUSA funds for this purpose, IDDI used \$90,922 of these funds to purchase two new vans, a central air-conditioning unit, and flooring in three of its program residences and its swimming pool area. Consequently, because the \$90,922 in LUSA funding was not used for its intended purpose, these payments to IDDI were unnecessary, unallowable, and inappropriate.

The DDS Purchase of Service Manual describes LUSAs and their purpose as follows:

DDS has established a distinctive contract methodology for purchasing intermittent, as-needed services for developmentally disabled individuals needing limited time placements. The purpose of LUSAs is to allow providers the opportunity to place on file with DDS a contract that can be accessed at any time during its life when an unexpected or limited time service is agreed upon by both the provider and DDS. LUSAs are not funded unless and until DDS and the provider agree on a service to be delivered.

DDS has developed an "Authorization for Services" form to establish the specific type of service, dates of service, and amount of funding allowed. This form describes appropriate use of LUSA funding as follows:

LUSA/MA billing is for additional services on an intermittent, as-needed limited time service that clients need due to specific circumstances that are not included in existing state-funded program contract.

We found that during fiscal year 2010, IDDI requested and received a total of \$90,922 in LUSA funding from DDS. However, rather than using these funds to pay for as-needed services for developmentally disabled individuals needing limited-use services, IDDI used these funds to purchase two new 2009 Ford E-250 vans, a central air-conditioning unit for its school building, and flooring in three program residences and its swimming pool area. IDDI officials stated that, at the end of fiscal year 2010, DDS officials contacted IDDI and instructed these officials to submit an invoice to DDS for any capital items that IDDI had purchased throughout the year

that were not funded through state contracts. IDDI submitted this list, and DDS reimbursed IDDI for these capital purchases using LUSA funds.

Regarding this matter, DDS's Northeast Regional Contract Manager confirmed that she did contact IDDI at the end of fiscal year 2010 and instructed IDDI to submit a payment voucher by June 30, 2010 for the aforementioned capital items. The Northeast Regional Contract Manager also acknowledged that the purpose of LUSA funds is to cover the cost of unanticipated emergency services vendors provided to consumers and stated that it was a mistake to use this funding to pay for capital items.

Recommendation

IDDI should consult with OSD and DDS to resolve the unallowable capital purchases paid for with LUSA funds. In addition, IDDI should ensure that any LUSA funding received in the future is expended in accordance with LUSA contract regulations.

Auditee's Response

In response to this issue, IDDI's Chief Executive Officer stated, in part:

This comment reads as if the Organization was aware that DDS was providing funding from an inappropriate source. The Organization acted in good faith in executing the contract. We simply submitted an invoice that clearly indicated it was for "Capital Budget for Fiscal Year 2010" as directly requested by DDS. Please note the Organization has reasonably relied upon the receipt of these funds in making decisions about subsequent capital expenditures.

Auditor's Reply

Although IDDI did not initiate this transaction, IDDI is responsible for being aware of and adhering to all state regulations, including those relating to the purchasing of capital items and the use of LUSA funding. In this regard, when a vendor identifies capital purchases to be made, the vendor is required to follow a process that includes submitting special capital budget forms for approval by the state purchasing agency. As stated in our report, LUSA funding is not intended to be used for the purchase of capital items, and IDDI should ensure that, in the future, it only uses LUSA funding for its intended purposes and that it follows the established process for requesting funding for the purchase of capital items. It should be noted that the Office of the State Auditor will be issuing a separate report on DDS's administration of LUSA funding.

3. UNALLOWABLE FRINGE BENEFITS TOTALING \$23,839

Our audit revealed that during our audit period, IDDI provided certain employees with \$23,839 in unallowable fringe benefits. Specifically, we found that IDDI (a) charged \$11,739 in expenses associated with company-owned/-leased vehicles provided to its Executive Director, Chief Financial Officer (CFO), and Director of Development for their personal and business use and (b) provided loans to seven employees totaling \$12,100. Under 808 CMR 1.05(9), OSD defines certain costs that are unallowable and nonreimbursable under state contracts, as follows:

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.

Because these fringe benefits that IDDI provided to certain staff members were not available to all staff members under an established agency policy, they were unallowable and nonreimbursable, as discussed below:

a. Unallowable Vehicle Expenses Totaling \$11,739

During our audit period, IDDI provided three members of its administrative staff with the following company-owned vehicles for their personal and business use:

Vehicle Descriptions and Assignments

Fiscal Year 2010

<u>Vehicle Type</u>	<u>Assigned to</u>
2008 GMC Denali	Chief Financial Officer
2009 Nissan Murano	Executive Director
2010 Nissan Maxima	Director of Development

Only fiscal year 2010 documentation relative to vehicle expenses was available for our review.¹ Based on IDDI's records, IDDI charged the following vehicle-related expenses, excluding gasoline:

¹ During fiscal year 2011, IDDI reported over \$18,000 in expenses associated with these vehicles as nonreimbursable costs in its UFR.

Agency-Assigned Vehicle Costs

Incurred by IDDI during Fiscal Year 2010

<u>Vehicle Expense Description</u>	<u>Amount</u>
Depreciation	\$11,345
Vehicle Lease Payments	6,600
Insurance	3,068
Maintenance	<u>851</u>
Subtotal	21,864
Less: Reported Nonreimbursable	
Expenses (personal use)	<u>(10,125)</u>
Total	<u>\$11,739</u>

Our review of the internal controls that IDDI had established over the use of these vehicles, as well as the documentation of expenses associated with these vehicles, noted the following issues:

- During our audit period, IDDI did not have policies and procedures requiring it to maintain a record of the business versus personal use of these vehicles. Because IDDI could not provide any such supporting documentation (e.g., travel logs, work schedules), it was not possible to determine the extent to which these vehicles were used for business and personal purposes. Therefore, the personal use deduction reported as nonreimbursable expenses in fiscal year 2010 could not be verified.
- IDDI's policies and procedures did not offer this fringe benefit to all employees. Consequently, IDDI's expenses associated with the provision of this fringe benefit are nonreimbursable in accordance with 808 CMR 1.05(9).

During our audit, we brought this matter to the attention of IDDI officials, who acknowledged that IDDI lacked written controls over agency-assigned vehicles. However, these officials stated that IDDI was in the process of developing policies and procedures in this area that will include requiring drivers to keep a log of their personal and business use of the vehicles.

b. Unallowable Employee Loans Totaling \$12,100

From October 2, 2009 through April 6, 2011, IDDI loaned a total of \$12,100 to seven of its employees, including its Director of Human Resources, its Director of Development, and various administrative and program staff members. For each loan, IDDI executed a written

agreement between itself and the employee that required each employee to repay the loan over a specified period of time through payroll deductions. The \$12,100 in loans provided to these seven staff members was ultimately repaid by these individuals. However, IDDI did not charge interest or administrative fees for any of these loans. Further, because the provision of staff loans was not an established written policy of the agency available to all employees, any state funds that were used to provide these loans to these individuals represent nonreimbursable expenses.

During our audit, we brought this matter to the attention of IDDI officials, who informed us that IDDI has discontinued the practice of providing loans to staff members.

Recommendation

IDDI should ensure that it does not use state funds to provide loans to staff members. Further, IDDI should remit to the Commonwealth the \$11,739 in unallowable vehicle expenses we identified during our audit and ensure that it does not charge any unallowable vehicle expenses against its state contracts.

Auditee's Response

In response to this issue, IDDI's Chief Executive Officer stated, in part:

These amounts [loans] were never charged to an expense, as they were reported as an asset in the Organization's financial statements and thus were not funded with state funds.

Auditor's Reply

The OSA is aware that the funds used to provide the loans to the employees in question were not directly expensed to state contracts. However, these loans were funded by IDDI's general operating account, which did contain state funds. Since the loans were repaid, the OSA is not requesting reimbursement of these funds. However, our concern is that IDDI provided loans to certain employees without a formal policy approved by its board that provided for this benefit. Based on its comments, IDDI has discontinued its practice of providing loans to staff members.

4. UNALLOWABLE PROGRAM EXPENSES TOTALING \$13,200 CHARGED TO STATE-FUNDED CONTRACTS

Between September 1, 2008 and March 31, 2011, IDDI leased an apartment to its former Executive Director that was located within a building used to house consumers in its state-funded Adult Residential Program. During this period, IDDI received a total of \$18,600 in rental income from its former Executive Director. According to state regulations, any non-state contract revenues received in state-funded programs should be used to offset the state's cost of operating the program. However, during fiscal years 2009 and 2010, IDDI received a total of \$13,200 and did not use this revenue to offset the state's cost of operating this program. Rather, IDDI reported this income as "other revenue" and used these funds to offset nonreimbursable expenses it had charged against its state-funded contracts, resulting in unallowable expenses totaling \$13,200.

When negotiating contracts with state purchasing agencies, human service providers such as IDDI are required to accurately identify any other sources of revenue available for their state-funded programs. Providers are required to use these additional revenues to offset the state's cost to operate the program. For example, if a program is budgeted to cost \$100,000 to operate and the provider anticipates collecting \$10,000 in client fees in the program, the provider can only request \$90,000 (\$100,000 - \$10,000) from the state purchasing agency.

OSD describes offsetting revenue in 808 CMR 1.02, as follows:

Off-Setting Revenue. The sum of the following revenues and support items. These revenues and support items must be received during the price year and must be dedicated for use in the same Program that also receives Commonwealth funds.

- (a) any Contractor revenues and support (including but not limited to public and private grants, gifts, contributions, bequests, or any income therefrom, income from endowments, funds received from the Massachusetts Department of Education's Bureau of Nutrition, or similar funding) to the extent that revenues and support are restricted to use in the Program;*
- (b) the amount of unrestricted revenues and support voluntarily designated by the Contractor to defray the cost of Program services to a Department;*
- (c) the fair market value of any public employees assigned to work in the Contractor's Program (including salaries, fringe benefits and travel allowances) and/or the occupancy of public facilities to the extent that they are available to the Program without charge or at less than fair market value;*

- (d) any revenues and support (including but not limited to Supplemental Social Security Income, Food Stamps, Emergency Aid to the Elderly, Disabled and Children (EAEDC), reimbursements from third-party payers, Client sliding fee scale payments) received by or available to the Contractor on account of Clients;*
- (e) the amount of Commercial Income that the Contractor or Department may designate;*
- (f) the value of revenues and support used to defray non-reimbursable costs; and*
- (g) not-for-profit Contractor surplus revenue retention funds accrued in excess of the limitations of 808 CMR 1.03(7) which may be utilized at the discretion of the Department to reduce the Authorized Price or Maximum Obligation of the Commonwealth.*

On September 1, 2008, IDDI began leasing an apartment to its former Executive Director that was located within a building housing consumers participating in its state-funded Adult Residential Program. According to IDDI officials, IDDI wished to have the former Executive Director available for late night coverage, late meetings, or other emergency situations that may arise during the operation of this 24-hour-per-day, 365-day-per-year residential care facility. Based on our analysis, the former Executive Director paid fair market value for the apartment lease.

According to IDDI's financial records, during the period in question, IDDI charged all of the costs associated with the operation of this apartment to its state-funded Adult Residential Program. However, we also determined that, contrary to OSD regulations, the rental income received from the Executive Director during fiscal years 2009 and 2010, which totaled \$13,200, was not used to offset the Commonwealth's costs of operating this program. Rather, we found that IDDI reported these rental payments as "other revenues" in its financial statements and used these funds to pay for nonreimbursable expenses billed against its state contracts during these fiscal years. As a result, IDDI received \$13,200 in excess funding from the Commonwealth. When this matter was brought to the attention of IDDI officials, the rental income IDDI received during fiscal year 2011 was applied to its Adult Residential Program expenses, as required by OSD.

According to IDDI's CFO, the rental income received from the former Executive Director was initially recorded by IDDI as Adult Residential Program revenue, but IDDI's independent auditor decided to subsequently report this income as other revenue. Nevertheless, IDDI's

management is responsible for ensuring that all IDDI revenue is accurately recorded, properly reported, and used for allowable purposes.

Recommendation

IDDI should remit to the Commonwealth the \$13,200 that it overbilled by failing to report the rental income received from its former Executive Director as revenue to its Adult Residential Program. Moreover, IDDI should ensure that all program income is accurately recorded and properly reported in accordance with state regulations.

Auditee's Response

In response to this issue, IDDI's Chief Executive Officer stated, in part:

[T]he final paragraph of the comment describes the CFO's representation of interaction with the independent auditor regarding this revenue. . . . The Organization had historically classified the revenue associated with the rental as administrative revenue because such revenue is non-program related.

Auditor's Reply

Contrary to state regulations, IDDI reported the rental income from its former Executive Director as "other revenue" rather than program revenue that was available to offset the state's cost of operating IDDI's Adult Residential Program. According to IDDI's financial records, during the period in question, IDDI charged all of the costs associated with the operation of this apartment to its state-funded Adult Residential Program, and therefore, in accordance with OSD regulations, the rental income received from the Executive Director should have been used to offset the Commonwealth's costs of operating this program. Consequently, IDDI overcharged the Commonwealth for the operation of this program during the period in question and should remit the \$13,200 in rental income to the Commonwealth.

5. UNNECESSARY EMPLOYEE COMPENSATION TOTALING \$38,792 CHARGED TO STATE-FUNDED CONTRACTS

During fiscal year 2010, IDDI's former Executive Director promoted a long-term employee, functioning as IDDI's Automotive Supervisor, to two newly created positions (first as Special Projects Manager and subsequently to Operations Director), thereby increasing this employee's annual salary from \$26,208 to \$65,000. During our audit, we reviewed the circumstances under which these positions were created and found that they may have been unnecessary. For

example, the position of Special Projects Manager did not exist prior to this employee's appointment and was eliminated approximately four months later. Also, the employee in question stated that, during the time he held this position, he did not initiate any special projects. Similarly, the position of Operations Director, which this individual held for 11 months, did not exist prior to this employee's appointment and was eliminated when he retired in December 2010. Consequently, we believe that the \$38,792 that IDDI charged against its state contracts for this employee's compensation while filling these positions was unnecessary and therefore nonreimbursable under IDDI's state contracts.

The 808 CMR 1.05, promulgated by OSD, identifies the following as nonreimbursable costs under state contracts:

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.

Moreover, 808 CMR 1.02 defines reimbursable operating costs as follows:

Reimbursable Operating Costs. Those costs reasonably incurred in providing the services described in the contract and/or, in the case of a Program approved under the provisions of M.G.L. c. 71B, in providing the services mandated by DOE or specifically included in an Authorized Price, with the exception of costs enumerated in 808 CMR 1.05 and costs excluded in the Authorized Price. 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 [OMB] Circular A-122 or A-21, or successors thereto.

Finally, OMB Circular A-122 defines reasonable operating 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. The question of the reasonableness of specific costs must be scrutinized with particular care in connection with organizations or separate divisions thereof which receive the preponderance of their support from awards made by Federal agencies. In determining the reasonableness of a given cost, consideration shall be given to:

- a. 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.*
- b. The restraints or requirements imposed by such factors as generally accepted sound business practices, arms length bargaining, Federal and State laws and regulations, and terms and conditions of the award.*

- c. 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.*
- d. Significant deviations from the established practices of the organization which may unjustifiably increase the award costs.*

According to the employee in question, on August 31, 2009 IDDI's former Executive Director promoted him from Automotive Supervisor to Special Projects Manager because IDDI had received some unanticipated funding that it wanted to use for various capital improvement projects. However, approximately four months later, IDDI's Executive Director recommended, and received the approval of the agency's Board of Directors, to promote this individual to the position of Operations Director effective January 1, 2010. On January 31, 2010, the Executive Director authorized a pay increase for this individual from \$26,208 to \$65,000 annually, and on December 10, 2010, this individual retired from IDDI.

During our audit, we attempted to assess IDDI's need for creating these two new positions. As IDDI had not developed a job description for the Special Projects Manager, it was not possible to compare this employee's qualifications to any job-related responsibilities that may have been associated with this new position. Additionally, it does not appear that any "special projects" were either initiated or completed during the four-month period when this individual held this position. Although this individual stated that the former Executive Director discussed with him various special projects to be funded with donations, such as installing train tracks throughout IDDI's grounds, building a memorial park dedicated to a deceased former Executive Director, and building a fishing dock, no such special projects were ever initiated.

Regarding the position of Operations Director, it appears that, rather than determining whether there was a need for this position and establishing qualifications to meet these needs, the former Executive Director developed the job description for this position to match the qualifications of the Special Projects Manager, who was a retired police officer. For example, the responsibilities of Operations Manager included participation in internal investigations, and the job description did not require any specific education or prior experience in the area of operations management. In contrast, the Facilities Manager, who reported to the Operations Director, was required to have a bachelor's degree or equivalent and at least five years of managerial/supervisory experience in the facilities management field. Further, based on other information we obtained,

it appeared that creation of the position of Operations Director was unnecessary for the following reasons:

- The process used to fill this position deviated from IDDI's normal hiring process. Specifically, IDDI did not conduct a job search for the most qualified candidate. Instead, the individual in question was simply appointed to this position.
- Prior to the appointment of the individual in question to this position, the tasks described in the job description for the Operations Director were effectively performed for several years by the agency's CFO. Therefore, the creation of this position represented a clear deviation from IDDI's established practices and resulted in the Commonwealth's paying more for the same services.
- The need for this position is also questionable because, on December 10, 2010, this individual retired from IDDI, and the position has since been eliminated.

Because the creation of these new positions was, in our opinion, unnecessary, the additional compensation provided to this individual while holding these positions represents \$33,570 in unallowable salary costs charged against IDDI's state contracts, as indicated in the table below:

Employee Compensation

August 31, 2009 through December 10, 2010

<u>Job Position</u>	<u>Term</u>	<u>Compensation Per Term</u>
Special Projects Director	8/31/09 through 12/31/09	\$ 9,072
Operations Director	1/1/10 through 12/10/10	<u>58,266</u>
	Total Compensation	\$67,338
Automotive Supervisor	8/31/09 through 12/10/10 (Projected)	<u>(33,768)</u>
	Difference	<u>\$33,570</u>

In addition to the \$33,570 noted above, we found that this individual also received \$5,222 in severance pay, bringing the total potentially excessive compensation he received to \$38,792.

According to IDDI officials, these job positions have been eliminated, but the positions will be revisited should the need arise in the future.

Recommendation

IDDI should remit to the Commonwealth the \$38,792 in unnecessary compensation it provided to the individual in question. In the future, IDDI should take measure to ensure that it does not charge any unnecessary expenses against its state contracts.

Auditee's Response

IDDI chose not to respond to this issue.

6. INAPPROPRIATE ALLOCATION OF \$9,335 IN FUNDRAISING EXPENSES TO STATE-FUNDED CONTRACTS

We found that IDDI charged \$9,335 in expenses associated with its fundraising activities against its state contracts during our audit period. Because state regulations prohibit human service providers from charging fundraising expenses against their state contracts, this \$9,335 represents an unallowable and nonreimbursable expense that should be remitted to the Commonwealth.

OSD has promulgated regulations that define certain costs as being unallowable and nonreimbursable by the Commonwealth. Specifically, 808 CMR 1.05(10) defines the following costs as nonreimbursable program costs:

Fundraising Expense. The cost of activities which have as their primary purpose the raising of capital or obtaining contributions, including the costs associated with financial campaigns, endowment drives, and solicitation of gifts and bequests.

We found that during fiscal year 2010, IDDI charged \$9,335 in expenses associated with its fundraising activities against its state contracts. IDDI's Director of Development performs a variety of administrative tasks for the agency, including its fundraising activities. The Director records the work he performs each day on a timesheet that lists three general activity areas: program, administrative, and fundraising. During our audit, we reviewed the Director of Development's timesheets for fiscal year 2010, compared this information with the amount of time IDDI's accounting department charged to each activity for this individual, and noted several problems. First, although the Director spent a certain percentage of administrative time (e.g., planning, answering e-mails, making telephone calls) on fundraising activities, IDDI's accounting department allocated 100% of the 407 hours he recorded as administrative time in his timesheets, which included all 248 hours of his paid leave time (i.e., vacation, sick, personal, and holiday leave), to state contracts rather than identifying an appropriate percentage of these

expenses as being associated with the Director's fundraising activities. Using the agency's allocation percentages, we calculated that 334 hours of the Director's administrative time should have been allocated to his fundraising activities.

In addition, according to the Director of Development's time records, IDDI charged 45 hours of his time that he spent directly working on fundraising activities, such as developing a fundraising report for IDDI's Board of Directors, to state contracts. This allocation resulted in IDDI's inappropriately charging its state contracts approximately \$9,335 (379 hours at \$24.63 per hour) during fiscal year 2010.

During our audit, we brought this matter to the attention of IDDI's CFO, who stated that in the future, he will ensure that all fundraising costs are identified and reported according to state contract regulations.

Recommendation

IDDI should remit \$9,335 to the Commonwealth for the inappropriate fundraising expenses charged to its state-funded contracts during fiscal year 2010. In addition, IDDI should implement policies and procedures to ensure that all future fundraising expenses are properly and accurately identified and reported in accordance with state contracts.

Auditee's Response

In response to this issue, IDDI's Chief Executive Officer stated, in part:

Based upon review of support provided by the state auditor, the amount indicated appears reasonable.

APPENDIX

Programs Operated by IDDI

Adult Residential Program

The Institute for Developmental Disabilities, Inc.'s (IDDI's) Adult Residential Program assists adults with severe developmental disabilities to develop skills that enhance their quality of life while becoming contributing members in the community. The program accomplishes its goals by:

- Encouraging and supporting community involvement;
- Supporting the development of an individual's talents and contributions to the community, home, friends, and family; and
- Supporting and assisting individuals in experiencing the pleasure and responsibility of everyday life.

Children's Program

IDDI's Children's Program is composed of two initiatives: schooling and residential services. The school provides a comprehensive environment for children under the age of 22 who have severe mental, physical, and behavioral disabilities. This school is designed to teach developmentally disabled children, adolescents, and young adults basic skills, which include eating, cooking, and basic hygiene. Residential services are provided for those who are unable to live at home due to the complexity of their disability and their need for 24-hour skilled care. The combination of these services helps to ensure a smooth transition for these children into an adult program.

Day Habilitation Program

The Day Habilitation Program is designed to meet the needs of the members of the Adult Program. Services are provided through individualized habilitation goals, which include fine motor skill and sensory skill development, cooking skills, and community involvement.