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INDEPENDENT STATE AUDITOR'S REPORT ON CERTAIN ACTIVITIES OF THE CENTER FOR SCHOOL CRISIS INTERVENTION AND ASSESSMENT, INC.

SEPTEMBER 1, 2004 THROUGH AUGUST 31, 2006

OFFICIAL AUDIT REPORT

JANUARY 24, 2007

TABLE OF CONTENTS/EXECUTIVE SUMMARY

The Center for School Crisis Intervention and Assessment, Inc. (Center School) was founded in 1994 as a for-profit organization for the purposes of operating a school for students with special needs and providing students with a community-based education. The Center School is regulated by the Department of Education (DOE) and provides educational assessment, school crisis intervention, therapeutic treatment and support to children and their families, and support for public schools in meeting the special needs of their students. During the period covered by our audit, the Center School employed 169 full-time staff and served approximately 85 students in its day school programs.

The scope of our audit was to examine various administrative and operational activities of the Center School during the period September 1, 2004 to August 31, 2006. Our audit was conducted in accordance with generally accepted government auditing standards for performance audits issued by the Comptroller General of the United States and included such audit procedures and tests as we considered necessary to meet these standards. Our audit procedures consisted of: (1) determining whether the Center School had implemented effective internal controls over its operations, and (2) assessing the school's business practices and its compliance with applicable laws, rules, regulations, and various fiscal and programmatic requirements of its state contracts.

Our audit identified Center School expenses totaling $162,020 that were unallowable in accordance with state regulations.

We found that between fiscal years 2003 and 2006, the Center School paid two consultants a total of $160,400 for business and legal consulting services. However, contrary to state regulations, the Center School did not procure these consulting services using a competitive bidding process or enter into formal written agreements with these consultants detailing each party's duties and responsibilities. Moreover, the Center School, in most instances, did not require these consultants to submit documentation to substantiate what services, if any, they actually provided. As a result, $157,200 of the $160,400 in consultant costs incurred by the Center School represents unallowable and nonreimbursable costs to the Commonwealth.

During the period October 31, 2003 through May 24, 2005, the Center School used $3,565 in public funds to make donations to various local fundraising events. According to state regulations, charitable contributions and donations are unallowable and represent non-reimbursable costs to the Commonwealth.

Our audit identified that the Center School reimbursed its Executive Director for undocumented expenses totaling $755. Specifically, during January 2005, the Executive Director and program staff took students snowboarding at local ski areas on six occasions. The Executive Director charged the cost of these trips to his personal credit card, for which he was later reimbursed $2,110. However, the Executive Director's credit card statement identified that the six trips only cost $1,355, or $755 less than his reimbursement.

Our audit found that the Center School used public funds totaling $500 to pay an accounting expense for JMC Food & Service Corporation (JMC), a related-party organization partially owned by the Executive Director. The expense was not applicable to the social service activities of the Center School. Therefore the $500 payment represents a non-reimbursable cost to the Commonwealth.

INTRODUCTION

Background

The Center for School Crisis Intervention and Assessment, Inc. (Center School) was founded in 1994 as a for-profit organization for the purposes of operating a school for students with special needs and providing them with a community-based education. The Center School is regulated by the Department of Education (DOE) and provides educational assessment, school crisis intervention, therapeutic treatment and support to children and their families, and support for public schools in meeting the special needs of their students. During the period covered by our audit, the Center School employed 169 full-time staff and served approximately 85 students in its day school programs.

The Center School's funding is derived primarily from student tuition payments made by local cities and towns. The Commonwealth's Operational Services Division (OSD), the state agency responsible for regulating the activities of special education schools such as the Center School, annually sets the school's tuition rate. For fiscal year 2006, the tuition rates established by OSD were $253 per day, or $55,654 per student per year, for its Elementary/Middle/High School program and $219 per day, or $48,122 per student per year, for its Transition program. Local cities and towns that enroll students at the Center School fund their tuition payments with money provided to them under the provisions of Chapter 70 of the Massachusetts General Laws, which they receive from the Commonwealth for primary and secondary education, including special needs education. Although the majority of the Center School's income is derived from these tuition payments, because it has its tuition rates set by OSD, it is subject to OSD regulations. During our audit period, the Center School received the following funding:

	Fiscal Year 2005	Fiscal Year 2006
Local Tuition Payments	$ 5,582,652	$ 5,287,701
Other Revenue	82,215	34,420
	$ 5,664,867	$ 5,322,121

Audit Scope, Objectives, and Methodology

The scope of our audit was to examine various administrative and operational activities of the Center School during the period September 1, 2004 to August 31, 2006. 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 the Center School had implemented effective internal controls, including:

    - Processes for planning, organizing, directing, and controlling program operations;
    - Policies and procedures to ensure that resource use is consistent with laws, rules, and regulations; and
    - Policies and procedures to ensure that resources are safeguarded and efficiently used.

2. An assessment of the Center School's business practices and its compliance with applicable laws, rules, and regulations, as well as the various fiscal requirements of its local service contracts.

In order to achieve our objectives, we first assessed the internal controls established and implemented by the Center School over its operations. The purpose of this assessment was to obtain an understanding of management's attitude, control environment, and the flow of transactions through the Center School's accounting system. We used this assessment in planning and performing our audit tests. We then held discussions with school officials and reviewed organization charts; internal policies and procedures; and applicable laws, rules and regulations. We also examined the Center School's financial statements, budgets, cost reports, and invoices to determine whether expenses incurred were reasonable; allowable; allocable; properly authorized and recorded; and in compliance with applicable laws, rules, and regulations.

Our audit was not conducted for the purposes of expressing an opinion on the Center School's financial statements. We also did not assess the quality and appropriateness of program services provided by the school under its special education programs. Rather, our objective was to report findings and conclusions on the extent of the Center School's compliance with applicable laws, rules, regulations, and contractual agreements and identify processes, methods, and internal controls that could be made more efficient and effective.

At the conclusion of our field work, we provided Center School officials with a copy of our draft audit report for their review and comments. We included in our report those comments made by the Center School that were relevant to issues presented in our report. A complete copy of the comments made by the Center School relative to our audit report is on file at the Office of the State Auditor.

AUDIT RESULTS

1. UNALLOWABLE CONSULTANT PAYMENTS TOTALING $157,200

We found that between fiscal years 2003 and 2006, the Center for School Crisis Intervention and Assessment, Inc. (Center School) paid two consultants a total of $160,400 for business and legal consulting services. However, contrary to state regulations, the Center School did not procure these consulting services using a competitive bidding process or enter into formal written agreements with these consultants that clearly defined the duties and responsibilities of each party. In addition, the Center School, for the most part, did not require the consultants to submit supporting documentation to substantiate what services if any, they provided. As a result, $157,200 of the Center School's consultant expenses represent unallowable and nonreimbursable costs to the Commonwealth.

The Commonwealth's Operational Services Division (OSD) has promulgated regulations applicable to special education schools such as the Center School that require entities contracting with the Commonwealth to use a competitive-bidding process when procuring goods and services. Specifically, 808 Code of Massachusetts Regulations (CMR) 1.03 (8) states:

> *(8) Procurement of Contractor Furnishings, Equipment and Other Goods and Services. 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.*

Additionally, OSD has promulgated regulations that define certain costs as being unallowable and nonreimbursable costs to the Commonwealth. Specifically, 808 CMR 1.05 (26) defines the following costs as nonreimbursable program costs:

> *(26) Undocumented Expenses. Costs which are not adequately documented in the light of the American Institute of Certified Public Accountants statements on Auditing standards for evidential matters.*

During the four-year period ended August 31, 2006, the Center School procured business and legal services totaling $160,400 from two consultants. However, our audit found that the Center School selected both consultants based upon factors other than open and free competition, contrary to OSD regulations. The business consultant was selected based upon a recommendation made by a business associate of the Center School's Executive Director, whereas the Center School decided to utilize the Secretary to its Board of Directors as its legal consultant. In addition, the Center School did not enter into formal written agreements with these consultants to document the terms and conditions of their consultant services, including scope of services, maximum obligation, and service delivery period. Lastly, the Center School, in most instances, did not maintain documentation such as billing invoices and service reports to ensure the delivery of these consultant services and support the expenditure of public funds. In this regard, consultant payments totaled $160,400 for the four-year period ended August 31, 2006, but the Center School maintained documentation to support only $3,200 of these expenses. Therefore, the total amount of undocumented consultant payments for the period was $157,200. The following table details the Center School's unallowable consultant payments over the four fiscal years ended August 31, 2006:

Fiscal Year	Business Consultant	Legal	Total
2003	$ 24,000	$ 23,000	$ 47,000
2004	24,000	18,000	42,000
2005	19,953	9,247	29,200
2006	21,000	18,000	39,000
Total	$ 88,953	$ 68,247	$157,200

During the audit, Center School officials provided the following information relative to the hiring and services of the business consultant.

- The Center School hired the business consultant several years ago and, at the time, the Executive Director did not believe it was necessary to have a formal agreement detailing the business consultant's scope of services, contract term, rate of compensation, or maximum obligation.

- The Executive Director made a verbal agreement with the business consultant under which the business consultant was not required to submit invoices to substantiate his $2,000 monthly fee.

- The business consultant assisted the Center School with new program development, community outreach, and other business matters. However, the Center School could not provided us copies of the business consultant's service reports or products and the Executive Director could describe only one specific example of his work for the four-year period ended August 31, 2006.

Our review found similar problems with the Center School's legal consultant. According to the Executive Director, the legal consultant receives a monthly retainer fee of $1,500, which provides for approximately 10 hours of legal service each month on behalf of the school. However, the Center School could not produce a signed agreement detailing the legal consultant's responsibilities and rate of compensation. Furthermore, the Center School's Financial Officer stated that the legal consultant only submits invoices when his works for the school exceed 10 hours per month. Our review of the Center School's records identified that the legal consultant received $71,447 over the four-year period ended August 31, 2006. However, contrary to OSD regulations, the Center School maintained documentation to support legal expenses totaling only $3,200, or 4.5%, of this amount.

Recommendation

In order to address our concerns relative to this matter, we recommend that the Commonwealth recover the $157,200 in unallowable consultant expenses that the Center School incurred during the audit period and remit these funds in an equitable manner to the local communities who had students attending the school during the period covered by our audit. In the future, the Center School should develop policies and procedures to ensure that consultant services are awarded based upon free and open competition, that the agency enters into formal written contracts with all of its consultants, and that consultants' payments are supported by adequate documentation, as required by state regulations.

Auditee's Response

In response to this audit result, the Center School provided comments, which are excerpted below:

> *….The Center does not believe the amounts identified during the state audit for periods after August 31, 2005 should be included in the final state auditor's report. Financial reports for fiscal years subsequent to August 31, 2005 including the Uniform Financial Reports (UFR) have not yet been completed by the Center for that period. The Center School will reflect those non –reimbursable costs subsequent to August 31, 2005 as non-reimbursable costs in its Uniform Financial Report submitted to the Commonwealth as required by State regulations. To avoid a double jeopardy situation, with these items being resolved through your report and again by properly reporting these items in the UFR filing, I request that the amounts after August 31, 2005 be removed from your report….*

Auditor's Reply

In accordance with Chapter 11, Section 12 of the Massachusetts General Laws, and generally accepted government auditing standards issued by the Comptroller General of the United States, the Office of the State Auditor is responsible for issuing complete and accurate reports that communicate the results of each audit. In this case, the Center School utilized public funds totaling $157,200 for non-reimbursable consultant costs, of which $39,000 was expended during fiscal year 2006. By omitting the $39,000, as suggested by the Center School, the OSA would be providing report users with an incomplete picture of the Center School's activities during the audit period. In addition, while we appreciate the Center School's concern over "double jeopardy", the Operational Services Division, which is ultimately responsible for the state's audit resolution process, considers all pertinent information, including UFR reports, prior to making its decisions. Thus, the Center School is assured of receiving a fair and equitable disposition of the audit issues described in this report.

2. UNALLOWABLE DONATIONS TOTALING $3,565

During the period October 31, 2003 through May 24, 2005, the Center School used $3,565 in public funds to make donations to various local fundraising events. According to state regulations, donations constitute a luxury item, which are unallowable and a non-reimbursable cost to the Commonwealth.

The 808 CMR 1.05 (23), promulgated by OSD, identifies the following as nonreimbursable costs for special education schools such as the Center School.

> *Luxury Items. All costs associated with luxury items including but not limited to luxury passenger automobiles as defined in the Internal Revenue Service Code 4001 or 4002, airplanes, boats, vacation homes, alcoholic beverages, charitable contributions and donations, and all non-Program entertainment expenses.*

Despite this regulatory requirement, the Center School made donations ranging from $195 to $1,000 to local fire and police unions and various civic organizations. The Center School classified these donations within its General Ledger as recreational activities, office supplies, training and development, and employee benefits depending on the use of whatever nominal goods or services it received. Given the nominal value of the goods and services received, these expenditures should be classified as donations, which are non-reimbursable costs. The table below details the donations made by the Center School during the period October 31, 2003 to May 24, 2005.

Date	Check	Amount	Recipient	General Ledger Account
10/31/03	41343	$365	Chicopee Police Union	Recreational Activities
04/23/04	42150	425	Holyoke Merry Go Round	Training and Develop.
06/10/04	42432	1,000	Community Foundation	Office Supplies
08/16/04	42723	365	Springfield Firefighters	Recreational Activities
10/07/04	42969	365	Chicopee Patrolman's Union	Office Supplies
01/25/05	43529	350	Boys and Girls Club of Holyoke	Employee Benefits
03/25/05	43826	195	S. Hadley Police Department	Employee Benefits
05/24/05	44086	500	Holyoke Rotary Foundation	Office Supplies
		$3,565		

During our audit, we brought this matter to the attention of the Center School's Executive Director, who stated that when these expenditures were made, he believed that they were allowable contract costs. He added that in the future, he would take steps to ensure compliance with the state regulations regarding agency expenditures.

Recommendation

The Commonwealth should recover the $3,565 in public funds that the Center School used for unallowable donations and remit these funds in an equitable manner to the local communities who had students attending the school during the period covered by our audit. If the school wants to expend funds for these purposes in a manner that is not consistent with state regulations, it should identify these expenses as being nonreimbursable costs in the UFRs it files with OSD and follow OSD guidelines for reporting nonreimbursable costs.

3. UNDOCUMENTED EXPENSES TOTALING $755

Our audit identified that the Center School reimbursed its Executive Director $755 for undocumented student recreation expenses. According to state regulations, expenses that are undocumented are unallowable and nonreimbursable. Specifically, 808 CMR 1.05, promulgated by OSD, identifies the following expenses as nonreimbursable costs to the Commonwealth.

> *(26) Undocumented Expenses. Costs which are not adequately documented in the light of the American Institute of Certified Public Accountants statements on auditing standards for evidential matters.*

During the audit, we sample tested the Executive Director's credit card reimbursements for fiscal year 2005. Specifically, we examined reimbursements he received totaling $56,216 for office supplies, recreational activities, employee benefits, and telephone expenses. Although we found that almost all the expenses tested were adequately documented and accounted for, we did identify one questionable transaction totaling $755. In this regard, during January 2005, the Center School's Executive Director and program staff took students snowboarding at local ski areas on six separate occasions. The Executive Director charged the cost of these trips to his personal credit card, for which he was later reimbursed $2,110. However, the Executive Director's credit card statement identified that the six trips only cost $1,355, or $755 less than his reimbursement.

During our audit, the Center School's accounts payable clerk, who was responsible for processing this transaction, could only point to human error for the $755 variance. However, we believe that the problem resulted from the Executive Director's decision to utilize his personal credit card for both personal and business-related activities. For example, during January 2005, the Executive Director charged 58 items totaling $29,083 to his personal credit card. Of this amount, $8,662 represented Center School-related purchases; $6,366 represented expenses for three of the Executive Director's other business interests; and the remaining $14,055 represented the Executive Director's personal expenses. Other than the $755 for the month of January 2005, the audit did not identify any other costs for the Executive Director's credit cards that were improperly charged to the Center School's expenses from September 1, 2004 through August 31, 2006. Each month, the accounts payable clerk must reconcile the Executive Director's credit card statement and allocate his costs accordingly. The process can be confusing, and human error can lead to accounting problems such as the one noted above.

Recommendation

The Center School should recover the $755 in reimbursements it erroneously provided to its Executive Director. In addition, the Center School should establish a separate credit card account to ensure that state funds are properly accounted for and used solely for the Center School's special education programs. Moreover, the Center School should establish formal policies and procedures over the use of this credit card to ensure that all charges related to the Center School are fully documented and properly allocated to Center School programs.

Auditee's Response

In response to this audit result, the Center School provided comments, which are excerpted below:

> *It is the intent of the Center to directly return to each school system on a prorated basis, the amounts [determined to be undocumented].*

4. UNALLOWABLE RELATED PARTY COSTS TOTALING $500

Our audit found that the Center School used public funds totaling $500 to pay an expense of a company partially owned by the Executive Director. Specifically, on September 22, 2005, the Center School prepared a purchase order totaling $500 for food and materials from JMC Food & Service Corporation (JMC) a related party. Five days later, on September 27, 2005, the Center School issued a $500 check to JMC in full payment of the order. However, the Center School could not provide documentation (e.g., billing invoice, delivery receipt) to substantiate that JMC had actually delivered the ordered goods. Moreover, our audit identified that JMC used these funds to pay for the preparation of its annual tax return. In 808 Code of Massachusetts Regulations (CMR) 1.02, OSD has promulgated regulations that define a related party, as follows:

> *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).*

Moreover, Financial Accounting Standards Board (FASB) Statement No. 57, Related Party Disclosures, defines a related party as follows:

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

> *of the transacting parties might be prevented from fully pursuing its own separate interests.*

According to the Center School's fiscal year 2004 UFR filed with the Commonwealth, the Center School conducted business with a related-party, JMC, which was established to provide food services to the Center School. Moreover, according to Center School's records, the Center School's Executive Director and sole stockholder is also part owner of JMC.

Clearly, since this expense was not related to the programs and overall operation of the Center School, school funds should not have been used for this purpose. In this regard, OSD regulations identify expenses that are non-program-related as being nonreimbursable in 808 CMR 1.05 (12), which identifies the following as nonreimbursable costs:

> *Non-Program Expenses. Expenses of the Contractor which are not directly related to the social service Program purposes of the Contractor.*

Recommendation

The Center School should recover from its Executive Director the $500 that was provided to JMC. In the future, the Center School should take measures to ensure that it does not use public funds for such purposes. If the school wants to expend funds for these purposes in a manner that is not consistent with state regulations, it should identify these expenses as being nonreimbursable costs in the UFRs it files with OSD and follow the guidelines established by OSD for reporting nonreimbursable costs.

Auditee's Response

In response to this audit result, the Center School provided comments, which are excerpted below:

> *It is the intent of the Center to directly return to each school system on a prorated basis, the amounts [determined to be unallowable].*