



The Commonwealth of Massachusetts

AUDITOR OF THE COMMONWEALTH

ONE ASHBURTON PLACE, ROOM 1819
BOSTON, MASSACHUSETTS 02108

A. JOSEPH DeNUCCI
AUDITOR

TEL. (617) 727-6200

NO. 2009-4515-3C

**INDEPENDENT STATE AUDITOR'S REPORT
ON CERTAIN ACTIVITIES OF
THE EDUCATION COOPERATIVE
JULY 1, 2006 THROUGH FEBRUARY 28, 2009**

**OFFICIAL AUDIT
REPORT
APRIL 13, 2010**

TABLE OF CONTENTS/EXECUTIVE SUMMARY

INTRODUCTION

1

The Education Cooperative (TEC) was established in 1974 as an organization that provides educational services to certain school districts pursuant to Chapter 40, Section 4E, of the Massachusetts General Laws, which allows school districts, with the approval of the Commonwealth's Department of Elementary and Secondary Education (DESE), to enter into intergovernmental agreements establishing cooperative public entities referred to as education collaboratives. The statutory purpose of education collaboratives is "to conduct education programs and services which shall complement and strengthen the school programs of member school committees and increase educational opportunities for children."

TEC operates under the control of a Board of Directors composed of representatives selected by the school committees of each of its 16 member districts. During the period covered by our audit, TEC employed approximately 132 individuals, including part-time employees, and had revenues in excess of \$7.2 million. During this period, TEC's services included the operation of special education classrooms within member district schools, two free-standing alternative schools, vocational and other student transitional services, professional development services for educators, special programs such as a U.S. Department of Education grant-funded Teaching American History program for teachers, and a collective purchasing program for as many as 60 school districts, including its member districts. For most services, participation is open to both TEC's member districts and non-member districts and educators.

The scope of our audit included a review and examination of certain aspects of TEC's fiscal and programmatic operations during fiscal years 2007, 2008, and 2009 (through February 28, 2009). However, in some instances it was necessary to expand our audit period. 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. Our specific objectives were to review and assess the system of internal controls TEC has established over its operations and to conduct audit testing for the purposes of evaluating TEC's compliance with relevant laws, regulations, policies and grant and contract requirements.

During our audit, we identified in excess of \$334,000 in questionable expenditures including:

- At least \$148,933 in compensation arrangements for TEC's Executive Director and other TEC employees that appeared to be excessive or were not properly authorized;
- At least \$59,267 in questionable expenditures on food, alcohol, and meeting expenses related to school district Superintendent retreats at a Cape Cod resort, and various meetings and holiday parties;
- As much as \$125,832 in unbudgeted and inadequately disclosed expenditures for legislative agent services and other consultants.

Further, we found that, in some cases, TEC was not using properly licensed staff and was not in compliance with DESE regulations relative to conducting staff evaluations. Additionally, we determined that TEC had not established adequate budgeting, accounting, and service pricing practices, resulting in excessive charges to member and non-member school districts and the accumulation of over \$1.4 million in total net assets as of June 30, 2009. We also found deficiencies in the internal controls TEC had established over various aspects of its operations, such as staff attendance, documentation of agency expenses, telephone usage, and provisions for the return of funds to members upon their withdrawal from the collaborative. In addition, as discussed in the Other Matters section of our report, we determined that DESE could improve its oversight of TEC and other education collaboratives and that collective purchasing activities could be improved through coordination with the Commonwealth's Operational Services Division and the Office of the Inspector General.

AUDIT RESULTS

5

1. EXCESSIVE AND UNAUTHORIZED SALARY COMPENSATION AND FRINGE BENEFITS PROVIDED TO THE EXECUTIVE DIRECTOR AND OTHER TEC EMPLOYEES

5

Compensation and benefits for certain members of TEC's staff, including its Executive Director, appear to be excessive and/or not in accordance with the benefit levels approved by TEC's Board of Directors. For example, the Board of Directors provided the Executive Director with an annuity to supplement his salary even though TEC's own compensation survey documentation showed that the salary alone (\$154,157 in fiscal year 2008) exceeded the salaries for both larger education collaboratives in the Commonwealth and for many superintendents at TEC member districts. We projected that cumulative annuity costs to TEC would total approximately \$71,111 at the time of the Executive Director's planned June 30, 2009 retirement. In addition, shortly after his hiring in 2003 TEC's Executive Director authorized himself to receive a reimbursement check in lieu of participation in one of TEC's health insurance plan options. However, the reimbursement had not been provided for by his employment contract, and we found no documentation of board approval for this benefit. We estimate that during his six years of employment at TEC, the Executive Director received a total of \$44,520 in reimbursements from TEC for this benefit.

Although TEC has established a standard timesheet approval system for its hourly employees, TEC personnel systems are deficient in that they do not require managers to adequately document their work time and activities. Instead, TEC simply relies on managers to self-report any absences such as vacation or sick leave. Our audit found that personnel and payroll records did not document the use of any leave time by the Executive Director between July 1, 2008 and February 28, 2009. However, the appointment calendar maintained for the Executive Director by his Executive Secretary indicated that he had in fact taken at least 16 days of vacation during this period and that he was marked "out" for an additional 19 days. Further, based on our review of public information on the Internet, we found that for at least 9½ of the "out" days and for five additional days where his schedule had simply been left blank without reporting any absences or appointments, the Executive Director appeared to have been on location at

consulting engagements in Virginia and Louisiana, functioning as an employee for a private consulting company headquartered in Illinois that provides executive recruitment services.

We also found that TEC's Executive Director provided seven administrative staff members with salary increases that exceeded the annual raises authorized by TEC's board. During the spring of 2007, the board's Personnel Committee approved compensation levels for each staff position, including an across-the-board 3% salary increase for managers and administrative employees effective July 1, 2007. However, on October 4, 2007 TEC's Executive Director granted additional raises to seven administrative employees. The increases were made retroactive to July 1, 2007 and effectively provided actual pay increases between 7.5% and 16.1% per employee rather than the board-approved 3%, resulting in the unauthorized expenditure of approximately \$33,302 in excess compensation (excluding additional associated tax/fringe costs). Supplemental cell-phone and transportation "stipend" compensation was also provided to five managers. Since those employees were not required to document that they had incurred any actual expenses on behalf of TEC, the stipends, totaling \$7,320 for fiscal year 2008, constituted additional taxable employee compensation that had not been authorized by the TEC board.

Prior to March 14, 2008, TEC required employees to work for the agency for at least 10 years in order to be eligible for health insurance coverage upon retirement, at which time TEC would pay 50% of the premium costs of their coverage. This 10-year eligibility requirement is the same for all of TEC's member districts employees and for all public school district employees throughout the Commonwealth. However, we noted that on March 14, 2008, TEC's board eliminated the 10-year employment length of service eligibility requirement for TEC payment of the premium share amount. The revised eligibility criteria for this benefit requires no minimum length of service and simply requires the eligible retiree to have been enrolled in one of TEC's group health insurance plans for at least one school year prior to the date of retirement and be an actively enrolled participant at the time of retirement. This benefit change carries obvious financial implications for TEC and its member districts that can be significant; however, there is no documentation to substantiate that TEC's board fully analyzed the financial impact of this change prior to its implementation. Further, this change appears to be unnecessary and excessive in that it provides a greater level of benefits to TEC employees compared to those of other Massachusetts public school districts and agencies, which typically require that covered retirees have worked a combined total of at least 10 years at either the agency or other public agencies within the Commonwealth's public employee retirement systems.

Finally, we identified deficiencies in TEC's reporting of taxable compensation for the Executive Director and certain other managers, which had only partially been addressed before our completion of audit work. At least \$12,280 in taxable compensation, including at least \$8,620 for the Executive Director, had not been reported for calendar year 2008. TEC acknowledged that similar reporting omissions had occurred in prior years.

2. BUDGETING, ACCOUNTING, AND PROGRAM SERVICE PRICING DEFICIENCIES RESULTED IN INSUFFICIENT INFORMATION BEING PROVIDED TO TEC'S BOARD TO EFFECT PROPER OVERSIGHT AND QUESTIONABLE SURPLUSES IN EXCESS OF \$1.4 MILLION **22**

As a local governmental entity, TEC is required to establish systems that allow it to accurately budget and monitor its revenues and expenses and to develop detailed budget estimates so that it can establish accurate prices or fees for its program services. Accurate budget estimates and comparisons of budget to actual revenue and expense information are also essential for board oversight purposes. The Massachusetts Department of Revenue's Division of Local Services (DLS) and the state's Office of the Attorney General (OAG) have issued guidance relative to the amount of fees governmental agencies such as TEC can charge for their services. This guidance effectively states that the amount of fees a governmental agency should charge for services should not exceed its actual cost of providing the services. However, we found that TEC's budgeting, financial reporting, accounting, and pricing systems do not allow TEC's board to effect proper oversight of the agency and ensure proper accountability. Further, due to its inadequate accounting and budgetary controls, TEC has charged excessive fees to its member and non-member school districts, resulting in TEC's accumulating, over a multi-year period, a total of \$1,465,139 in total net assets (profits) of as of June 30, 2008, which is inconsistent with DLS and OAG guidance.

3. INADEQUATE CONTROLS OVER FOOD AND MEETING EXPENSES RESULTED IN AS MUCH AS \$59,267 IN UNNECESSARY AND UNALLOWABLE EXPENSES **40**

DOR, through DLS, has established guidance for all municipal governmental organizations, including education collaboratives, that recommends that these entities establish clear guidelines or policies relative to their allowable expenses. However, we found that during the period covered by our audit, TEC had not established such guidelines or policies. As a result, we determined that TEC incurred as much as \$59,267 in expenses for food and entertainment at Superintendent retreats and various other meetings and holiday parties that appeared to have been unnecessary and inconsistent with DLS guidance on allowable governmental expenses. Included in this amount is as much as \$1,809 for the purchase of alcohol at two Superintendent retreats, which is specifically prohibited by state law.

4. UNLICENSED OR INADEQUATELY QUALIFIED TEACHERS AND SERVICE AND SUPPORT STAFF **46**

According to Chapter 40, Section 4E, of the General Laws, certain categories of education collaborative employees, such as teachers, guidance counselors, and school psychologists, are required to be licensed by DESE. Other statutes provide for licensure by the Commonwealth's Division of Professional Licensure (DPL) for certain clinical professions such as occupational therapists. Despite these requirements, we found that during our audit period a number of TEC's staff did not meet these mandated licensing requirements. In some cases, TEC employees were simply not licensed, whereas in other cases, they were not properly licensed for the particular areas in which they were teaching. Specifically, during our review of the personnel records of 52 past or present TEC educators subject to DESE licensure requirements, we identified licensing issues for 29 of these 52 educators. In addition, we were unable to verify through TEC's

records that two other employees -- a speech therapist and an occupational therapist -- had been properly licensed by DPL. Finally, the special legal status of education collaboratives such as TEC has resulted in exceptions to licensing requirements for certain staff who would otherwise be required to have DESE licenses if they were working in regular public schools. Although education collaborative teachers must be licensed by DESE, their supervisors working in positions comparable to principals, department heads, special education administrators, and superintendents are generally exempt from DESE licensure requirements that would otherwise apply if they were working directly in a public school system. Collaborative Boards of Directors have the authority to establish qualification standards for these exempt employees, as well as supplemental standards for employees who are subject to DESE's licensure requirements. Nevertheless, we found that TEC and its board have not established a formal system of personnel policies, including job classifications and qualification requirements, for all its positions, including those not subject to DESE licensure. As a result, certain members of TEC's administrative staff may not have been held to the same job qualification standards that apply to staff working in public school districts and charter schools within the Commonwealth who hold similar positions.

5. NONCOMPLIANCE WITH STATE REGULATIONS RELATIVE TO THE EVALUATION OF TEACHERS AND ADMINISTRATORS

53

DESE regulations require education collaboratives such as TEC to develop appropriate employee performance standards and to conduct staff evaluations, which are to be documented in writing. According to these regulations, administrators and teachers without professional teacher status are to be evaluated at least annually, whereas those with professional status are to be evaluated at least once every two years. The stated purpose of these regulatory requirements is to ensure effective teaching and administrative leadership in the Commonwealth's public schools. However, we found that TEC had not established appropriate performance standards for its employees and that there was no documentation substantiating that TEC was conducting the required performance evaluations of its staff, including its Executive Director. Without such documentation, there is inadequate assurance that TEC is meeting its responsibilities to the Commonwealth.

6. TEC'S BOARD WAS NOT ADEQUATELY INFORMED OF AS MUCH AS \$125,832 IN CONSULTING EXPENDITURES, INCLUDING AS MUCH AS \$108,000 IN LEGISLATIVE AGENT SERVICES

56

According to its collaborative agreement, all TEC expenditures are required to be included in its annual budgets approved by its board or, where that has not been done, be expressly approved by the Board of Directors. However, we found that between July 1, 2006 and November 25, 2008, TEC managers expended at least \$113,832 (\$96,000 for legislative agent services and \$17,832 for legislative tracking and other outside consulting services) that had been excluded from board-approved budgets. All of these expenses were accounted for in TEC's accounting system in a non-budgeted account entitled "Government Consult." In addition, public disclosure filings made by TEC's legislative agent to the Public Records Division of the Commonwealth's Office of the Secretary of State indicated that an additional \$12,000 was expended for legislative agent services through December 31, 2008. TEC's Executive Director stated that although all these

expenditures were unbudgeted, he had obtained board approval for them. However, our review of the minutes of the meetings of TEC's board indicated that TEC's Executive Director advised the board that he was procuring legislative agent services only after he had contracted for them, and there was no indication in these minutes that the board formally approved any expenditure amounts for these services. In fact, according to its Chairperson, the TEC board was unaware that payments totaling \$96,000 for legislative agent services had been recorded in the general ledger through November 25, 2008. Moreover, the Chairperson stated that the board had been led to believe that these expenditures would total only approximately \$20,000. Although payments for these types of services are allowable under normal circumstances, the failure by TEC's administrative staff to include these expenditures in board-approved budgets or to properly document alternative board approval of these expenditures is a violation of the TEC collaborative agreement.

7. IMPROVEMENTS NEEDED IN INTERNAL CONTROLS OVER CERTAIN AGENCY ACTIVITIES

60

Generally accepted accounting principles require entities such as TEC to establish adequate internal controls over all aspects of their operation. Despite this, we found that during our audit period, TEC had not established adequate internal controls over several aspects of its operation. Specifically, TEC had not taken measures to adequately address all of the internal control deficiencies identified by its private accounting firms during recent audits, was not making sure it was conducting Criminal Offender Record Information (CORI) checks on certain employees every three years as required by state regulations, did not establish adequate systems to track the time each TEC employee spent working in each activity as required for state and federal accountability purposes, had not established adequate provisions for the return of funds to collaborative members upon their withdrawal from the collaborative, and had not established adequate controls over the use of its telephone systems. These internal control deficiencies can result in a variety of operational and administrative problems, including the potential loss or misuse of agency assets.

OTHER MATTERS

66

1. DESE IS NOT EFFECTIVELY MONITORING COLLABORATIVE ACTIVITIES

66

We found that DESE has not established policies and procedures to effectively monitor the activities of education collaboratives such as TEC. Although it has been statutorily assigned certain oversight responsibilities relative to collaborative activities, DESE has not updated the Education Collaborative Policy that it developed for this purpose since 1988. As a result, this policy is significantly outdated, and many of the oversight provisions detailed in the policy are no longer being implemented. Consequently, DESE does not have effective monitoring, financial reporting, and auditing systems for education collaboratives; does not ensure that a representative from DESE attends or participates in each collaborative's board meetings in an advisory capacity as required by state law, and has not adequately addressed issues regarding the applicability to collaboratives of various state laws and regulations that apply to public schools. This condition has resulted in education collaboratives not being held to the same

performance standards that apply to public school districts and charter schools within the Commonwealth.	
2. COLLECTIVE PURCHASING ACTIVITIES COULD BE IMPROVED THROUGH CONSULTATION WITH THE OPERATIONAL SERVICES DIVISION AND THE OFFICE OF THE INSPECTOR GENERAL	74
<hr/>	
TEC conducts collective purchasing of school, cafeteria, custodial, and athletic supplies, as well as fuel and natural gas, on behalf of as many as 60 Massachusetts school districts. Our audit indicated that these collective purchasing services appear to generate significant benefits and savings for participating districts. However, we believe that TEC should further consult and coordinate its procurement activities with the Commonwealth's Operational Services Division, which conducts similar statewide procurements open to participation by state and local government, and with the Office of the Inspector General, which oversees local government purchasing activities.	
<hr/>	
APPENDIX	79
<hr/>	
The Education Cooperative Governance	79
<hr/>	

INTRODUCTION

Background

The Education Cooperative (TEC) was established in 1974 as a governmental organization that provides educational services to certain school districts pursuant to Chapter 40, Section 4E, of the Massachusetts General Laws, which allows school districts, with the approval of the Commonwealth's Department of Elementary and Secondary Education (DESE), to enter into intergovernmental agreements establishing cooperative public entities referred to as education collaboratives. The statute states, in part:

Pursuant to the provisions hereof, two or more school committees of cities, towns and regional school districts may enter into a written agreement to conduct education programs and services which shall complement and strengthen the school programs of member school committees and increase educational opportunities for children.

TEC operates under the control of a Board of Directors composed of representatives selected by the school committees of each of its 16 member school districts (see Appendix). Although TEC's primary mission is to provide services to its member districts, the collaborative agreement between members allows TEC to also provide services to other districts. Although certain services are operated only for TEC members, most services are also open to non-member school districts on a fee-for-service basis. During the period covered by our audit, TEC operated the following services:

- Two special education networks - one providing education programs and services to children ages five to 22 with mild to moderate special needs, and one serving children ages three to 22 with moderate to severe special needs. These networks operate approximately a dozen special education classrooms, primarily located within TEC member district schools.
- A therapeutic continuum system composed of several classrooms located in member district schools. The classrooms educate children from kindergarten through middle school with social, emotional, or mental health issues.
- Two alternative schools - the Phoenix School and the TEC High School - operated on a freestanding basis separate from member school district facilities. The Phoenix School educates middle school and high school students with complex learning, behavioral, and emotional issues that necessitate a small, structured learning environment and offers both academic remediation and vocational programs leading to issuance of diplomas by each student's home school district. TEC High School provides secondary students of average to above-average intelligence with high-level academics and interactive experiences while helping them overcome academic, emotional, and personal issues that have interfered with their past school experiences.

- Other related direct education services for students transitioning from high school settings to community-based adult living experiences; a high school based learning and vocational center for students with moderate developmental delays; a separate vocational training program for high school and post-secondary students with special needs; and coordination of unpaid work experience internships for students who have completed at least the first two years of high school, as well as for post-secondary students.
- Professional development and licensure services for both educators and administrators. Licensure programs are operated in partnership with Framingham State College and Boston University, with both employees and outside consultants used to conduct professional development classes.
- Grant programs funded from state, federal, and private grantors for a variety of purposes, including a U.S. Department of Education “Teaching American History” grant funded under Title II-C, Subpart 4, of the Elementary and Secondary Education Act. The goal of that grant is to indirectly raise student achievement by improving teachers’ knowledge, understanding, and appreciation of American history.
- Procurement management services for the collective purchasing of school district goods and services. TEC refers to its collective purchasing program as “cooperative purchasing” and annually conducts six public bid solicitations on behalf of both its members and as many as 45 non-member school districts for office and classroom supplies, food services supplies, athletic equipment and supplies, custodial supplies, fuel oil, and natural gas.

TEC’s revenue primarily comes from annual assessments to its member schools districts and from tuition payments charged by TEC to both TEC members and non-members on a student- and program-specific basis. TEC also collects other fees such as those charged to both contractors and school districts participating in its cooperative purchasing system. Also, certain services such as professional development, licensure, and internship programs, may be directly charged by TEC to individual educators and students. TEC also receives funding from state, federal, and private grants for specific purposes. For fiscal year 2008, TEC had 132 full- or part-time employees and received revenues totaling over \$7.2 million in revenue, as detailed below:

<u>REVENUE SOURCE</u>	<u>AMOUNT</u>
Tuitions	\$5,000,397
Member Assessments	342,101
Therapy and Aides Income	533,844
Licensure Income	208,915
Governmental Revenue	467,356
Professional Development Income	410,963
Registration Income	134,329
Contributions and Other Income	<u>132,066</u>
Total Revenue*	<u>\$7,229,971</u>

**Source: TEC’s audited financial statements for the year ended June 30, 2008. The audited financial statements provided to us by TEC managers reported each revenue amount as stated in the table but incorrectly reported the total as \$7,230,011.*

Audit Scope, Objectives, and Methodology

The scope of our audit included a review and examination of certain aspects of TEC's fiscal and program operations during fiscal years 2007, 2008, and 2009 (through February 28, 2009). However, in some instances it was necessary to expand our audit period. 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, which consisted of the following:

- To review and assess the system of internal controls TEC has established over its operations.
- To conduct audit testing for the purposes of evaluating TEC's compliance with relevant laws, regulations, policies, and grant and contract requirements.

To achieve our objectives, we first reviewed applicable laws, regulations, agency policies and procedures, and other guidance relative to education collaborative activities that have been issued by various state agencies. We then spoke with representatives from DESE; the Executive Director of the Massachusetts Organization of Educational Collaboratives; various TEC staff members, including; its Executive Director, Assistant Executive Director, Administrator of Finance and Operations, and Treasurer; and the Chairperson of TEC's Board of Directors. We observed various agency activities to obtain an understanding of how TEC operates and examined TEC's financial and personnel records to assess the adequacy of control systems and the reasonableness of various transactions, as well as TEC's compliance with various contractual, statutory, and regulatory requirements.

During our audit, we identified in excess of \$334,000 in questionable expenditures, including:

- At least \$148,933 in compensation arrangements for TEC's Executive Director and other TEC employees that appeared to be excessive or were not properly authorized
- At least \$59,267 in questionable expenditures on food, alcohol, and meeting expenses related to school district Superintendent retreats at a Cape Cod resort, and various meetings and holiday parties
- As much as \$125,832 in unbudgeted and inadequately disclosed expenditures for legislative agent services and other consultants

Further, we found that, in some cases, TEC was not using properly licensed staff and was not in compliance with DESE regulations relative to conducting staff evaluations. Additionally, we determined that TEC had not established adequate budgeting, accounting, and service pricing practices, resulting in excessive charges to member and non-member school districts and the accumulation of over \$1.4 million in total net assets as of June 30, 2009. We also found deficiencies in the internal controls TEC had established over various aspects of its operations, such as staff attendance, documentation of agency expenses, telephone usage, provisions for the return of funds to members upon their withdrawal from the collaborative. In addition, as discussed in the Other Matters section of our report, we determined that DESE could improve its oversight of TEC and other education collaboratives and that collective purchasing activities could be improved through coordination with the Commonwealth's Operational Services Division and the Office of the Inspector General.

On June 30, 2009, TEC's Executive Director retired from the agency and was replaced by a new Executive Director who had been employed at TEC in the positions of Administrator of Student Services and Assistant Executive Director during the period covered by our audit. Consequently, all references to TEC's Executive Director in this report refer to the individual employed by TEC in this position during the period covered by our audit and not to TEC's current Executive Director.

AUDIT RESULTS

1. EXCESSIVE AND UNAUTHORIZED SALARY COMPENSATION AND FRINGE BENEFITS PROVIDED TO THE EXECUTIVE DIRECTOR AND OTHER TEC EMPLOYEES

Compensation and benefits for certain members of TEC's staff, including its Executive Director, appear to be excessive and/or not in accordance with the benefit levels approved by TEC's Board of Directors. For example, the Board of Directors provided the Executive Director with an annuity to supplement his salary even though TEC's own compensation survey documentation showed that the salary alone (\$154,157 in fiscal year 2008) exceeded the salaries for both larger education collaboratives in the Commonwealth and for many superintendents at TEC member districts. We projected that cumulative annuity costs to TEC would total approximately \$71,111 at the time of the Executive Director's planned June 30, 2009 retirement. In addition, shortly after his hiring in 2003 TEC's Executive Director authorized himself to receive a reimbursement check in lieu of participation in one of TEC's health insurance plan options. However, the reimbursement had not been provided for by his employment contract, and we found no documentation of board approval for the \$635 per month benefit (fiscal year 2008 amount). We estimate that during his six years of employment at TEC, the Executive Director received a total of \$44,520 in reimbursements from TEC for this benefit.

Although TEC has established a standard timesheet approval system for its hourly employees, TEC personnel systems are deficient in that they do not require managers to adequately document their work time and activities. Instead, TEC simply relies on managers to self-report any absences such as vacation or sick leave. Our audit found that personnel and payroll records did not document the use of any leave time by the Executive Director between July 1, 2008 and February 28, 2009. However, the appointment calendar maintained for the Executive Director by his Executive Secretary indicated that he had in fact taken at least 16 days of vacation during this period and that he was marked "out" for an additional 19 days. Further, based on our review of public information on the Internet, we found that for at least 9½ of the "out" days and for five additional days where his schedule had simply been left blank without reporting any absences or appointments, the Executive Director appeared to have been on-location at consulting engagements in Virginia and Louisiana, functioning as an employee for a private consulting company headquartered in Illinois that provides executive recruitment services.

We also found that TEC's Executive Director provided seven administrative staff members with salary increases that exceeded the annual raises authorized by TEC's board. During the spring of 2007, the board's Personnel Committee approved compensation levels for each staff position, including an across-the-board 3% salary increase for managers and administrative employees effective July 1, 2007. However, on October 4, 2007 TEC's Executive Director granted additional raises to seven administrative employees. The increases were made retroactive to July 1, 2007 and effectively provided actual pay increases between 7.5% and 16.1% per employee rather than the board-approved 3%, resulting in the unauthorized expenditure of approximately \$33,302 in excess compensation (excluding additional associated tax/fringe costs). Supplemental cell-phone and transportation "stipend" compensation was also provided to five managers. Since those employees were not required to document that they had incurred any actual expenses on behalf of TEC, the stipends, totaling \$7,320 for fiscal year 2008, constituted additional taxable employee compensation that had not been authorized by the TEC board.

Prior to March 14, 2008, TEC required employees to work for the agency for at least 10 years in order to be eligible for health insurance coverage upon retirement, at which time TEC would pay 50% of the premium costs of their coverage. This 10-year eligibility requirement is the same for all of TEC's member districts employees and for all public school district employees throughout the Commonwealth. However, we noted that on March 14, 2008, TEC's board eliminated the 10-year employment length of service eligibility requirement for TEC payment of the premium share amount. The revised eligibility criteria for this benefit requires no minimum length of service and simply requires the eligible retiree to have been enrolled in one of TEC's group health insurance plans for at least one school year prior to the date of retirement and be an actively enrolled participant at the time of retirement. This benefit change carries obvious financial implications for TEC and its member districts that can be significant; however, there is no documentation to substantiate that TEC's board fully analyzed the financial impact of this change prior to its implementation. Further, this change appears to be unnecessary and excessive in that it provides a greater level of benefits to TEC employees compared to those of other Massachusetts public school districts and agencies, which typically require that covered retirees have worked a combined total of at least 10 years at either the agency or other public agencies within the Commonwealth's public employee retirement systems.

Finally, we identified deficiencies in TEC's reporting of taxable compensation for the Executive Director and certain other managers, which had only partially been addressed before our completion of audit work. At least \$12,280 in taxable compensation, including at least \$8,620 for the Executive Director, had not been reported for calendar year 2008. TEC acknowledged that similar reporting omissions had occurred in prior years. The specific issues we identified appear below:

a. Potentially Excessive and Unallowable Fringe Benefits Totaling as Much as \$115,000 Provided to TEC's Executive Director

Effective July 1, 2003, TEC entered into an employment contract with its Executive Director. The provisions in this contract covered the terms and conditions of his employment, including his salary, paid leave time, travel, professional dues allowances, and other fringe benefits as adopted by TEC's Board of Directors. During our audit, we compared the terms and conditions of the Executive Director's employment contract, as well as any amendments to this contract, to the level of compensation and fringe benefits he received and noted the following issues:

Potentially Excessive Retirement Fund Compensation Totaling \$71,111 Provided to TEC's Executive Director

During our review of TEC's Executive Director's personnel file, we noted a copy of a June 2, 2006 memorandum from the Personnel Committee of TEC's board to the full board, which states, in part:

Last year the Executive Director brought to our attention a significant problem relative to his participation in the Massachusetts Teachers Retirement System. Participation in the system is mandatory for him at a rate of 11% of his annual salary. Unfortunately he will receive no benefits from the system unless he stays in the system for 10 years, which he does not intend to do. His money will be returned to him with no interest accrued at the time he leaves the system.

In order to create "a retirement system" for him, the Board, last year, agreed to match a portion of the 11% during the two ensuing years (50% in 2005 [fiscal year 2006] and 75% in 2006 [fiscal year 2007]) followed by 100% matching of the 11% the third year and all subsequent years of his employment. . . . As a result of our actions last year, a supplement to his 11% retirement contribution was given to the Executive Director for the third and all subsequent years of his employment at TEC. The first two years of his employment did not include such a supplement. In order to provide a supplement for one additional year, we are recommending that June 30 of each year be the date of the supplement instead of July 1. Thus the supplement for each year will be paid retroactively instead of prospectively.

As a result of these additional retirement system contributions, TEC's Executive Director, in addition to being refunded all of his contributions to the Massachusetts Teachers Retirement System, also received a total of approximately \$71,111 in supplemental compensation as of June 30, 2009. In our opinion, since this benefit is not offered to any other TEC employee, the provision of this benefit was excessive and discriminatory in nature.

We acknowledge that it is necessary for organizations such as TEC to establish levels of compensation sufficient to attract and retain competent staff. However, a 2008 salary survey of 27 Massachusetts education collaboratives that was provided to us by TEC officials indicated that the salary of TEC's Executive Director for that year, which was \$154,157, was at least \$7,600 higher than the salary of any other Executive Director employed by the education collaboratives surveyed, despite the fact that 18 of the 27 surveyed collaboratives were larger than TEC, some having budgets three times larger than TEC's. The Executive Director's salary also exceeded the salary for at least five of the Superintendents in TEC's member districts. The need to provide this additional retirement benefit to the Executive Director is also questionable, given that he was also receiving retirement benefits as the result of his past two retirements from Superintendent positions in Texas and New York State.

TEC's Executive Director Received an Estimated \$44,520 in Health Care Benefits That Were Not Formally Authorized by His Employment Contract or TEC's Board of Directors

One of the fringe benefits that TEC employees are offered is health insurance coverage that is partially paid for by TEC. TEC's Executive Director's employment contract provided that he be allowed to participate in one of TEC's health insurance plans by stating, "The Executive Director shall be entitled to all insurance plans (medical, hospital, life, etc.) adopted by the Board for the employees of TEC." The Executive Director's contract did not include any special provisions for any form of reimbursed health insurance coverage other than the group health insurance plans available to TEC's other employees. Despite this, during our review of the Executive Director's personnel file we found that, unlike other TEC employees, the Executive Director was receiving a reimbursement check of \$635 per month to cover his share of the premium on a family health plan provided by a previous employer in the state of Texas. According TEC's personnel records, these alternative health coverage arrangements were implemented by the Executive Director on August 14, 2003, were made retroactive to his first day of employment on July 1, 2003 and would total a projected \$44,520

as his date of retirement on June 30, 2009. Despite the implementation of these special health insurance reimbursement arrangements, no corresponding changes had been made to the Executive Director's employment contract to authorize these payments, and there was no documentation in the minutes of the meetings of TEC's board that substantiated that the board ever formally approved this benefit. Since this benefit was not provided for by either the Executive Director's employment contract or accepted agency practices and was not formally authorized by TEC's board, the propriety of the \$44,520 in reimbursements is questionable.

Inadequate Controls over Time and Attendance Resulting in the Potential Unrecorded Use of Leave Time by TEC's Executive Director

During our audit, we identified deficiencies in the process TEC uses in accounting for the attendance of some of its employees. Specifically, although TEC has established a standard timesheet approval system for hourly employees such as its clerical staff and classroom aides, TEC relies on a reporting by exception approach for its administrators. This approach assumes that employees are present and working unless these employees or their supervisors report their absences to TEC's payroll office, which is responsible for tracking leave usage and making payroll and accounting expense classification adjustments. During our audit, we identified discrepancies in two different sets of agency records regarding the attendance of TEC's Executive Director. Specifically, TEC's payroll records did not document any absences for the Executive Director during the period July 1, 2006 through February 28, 2009. However, a separate appointment calendar maintained by his Executive Secretary documented that, during this period of time, the Executive Director had numerous absences, sometimes labeled on the schedule as "vacation" and other times labeled simply as "out." The appointment calendar had 16 days during this period that were labeled as vacation days even though they had apparently not been reported to TEC's payroll unit by either the Executive Director or his Secretary. And for 43.5 other days, the calendar indicated that the Executive Director was simply "out," with no further explanation. Appointments had been documented for only 124 days, and for approximately 462.5 operational days, the Executive Director's schedule was simply left blank. The results of our analysis of the appointment calendar for the Executive Director during the period in question is summarized in the following table:

TEC Executive Director Attendance/Work Schedule

July 1, 2006 through February 28, 2009

Period	Days with Appointments	Vacation Days	"Out" Days	Blank Operational Days
July 1, 2008 - February 28, 2009	21	16	19	106
July 1, 2007 – June 30, 2008	53	0	20.5	166
July 1, 2006 – June 30, 2007	<u>50</u>	<u>0</u>	<u>4</u>	<u>190.5</u>
Total	<u>124</u>	<u>16</u>	<u>43.5</u>	<u>462.5</u>

The conflict in information between TEC's payroll records and his appointment calendar clearly calls into question the accuracy of the leave records maintained by TEC's payroll unit for the Executive Director.

Moreover, during our audit TEC's Executive Director stated that he is also engaged in private consulting work for an executive recruitment firm, Hazard, Young, Attea and Associates, Ltd. (HYAA) of Glenview, Illinois. According to the firm's Internet site, he joined the firm in 2001 and is currently a board officer and senior associate. Information posted by HYAA on its Internet web site, as well as other publicly available Internet-based documents such as school committee meeting minutes, indicate that the Executive Director may have been providing consulting services on days when TEC's payroll records indicate that he was being paid for working at TEC. For example, based on our review of public information on the Internet, we found that during at least 9½ days between July 1, 2008 through February 28, 2009, when TEC's Executive Director's attendance was labeled as "out" in his appointment calendar but for which TEC's payroll records recorded no absences, the Executive Director may have in fact been on location at consulting engagements in Virginia Beach, Virginia; Arlington, Virginia; and East Baton Rouge, Louisiana on behalf of HYAA. In addition, for at least five days for which the Executive Director's schedule had been left blank, Internet-based documentation indicates that the Executive Director may also have been at consulting engagements on behalf of HYAA. For example, the Executive Director's appointment calendar had been left blank regarding his whereabouts on Friday, August 1, 2008, but school committee minutes for the Virginia Beach

City School District documented the Executive Director's presence there at the start of a 6:00 PM meeting on that day. Similarly, his Executive Secretary's schedule had been left blank regarding his whereabouts between November 24 and 26, 2008; however, according to Internet-based information, the Executive Director was involved in a meeting in Arlington, Virginia on November 24, 2008.

b. Compensation Arrangements Were Provided to Certain TEC Employees That Were Not Consistent with Agency Practices, and during Fiscal Year 2008, TEC's Executive Director Provided Retroactive Raises to Seven Administrative Staff Members Ranging from 7.5% to 16.1% That Exceeded the 3% Pay Increase Authorized by TEC's Board

During our audit period, TEC had not promulgated formal personnel policies and procedures for distribution to all of its employees. Rather, we found that TEC's employees are periodically given personnel information verbally and in the form of handouts. We reviewed these handouts and noted that they do not cover all positions and employment arrangements. We also determined that TEC's personnel unit maintained separate compensation and benefit schedule spreadsheets that contained conflicting information for some positions. Moreover, the level of benefits actually provided to staff often conflict with the information included in handouts and internal schedules, and even with the provisions of some staff's employment contracts and various provisions approved by TEC's board. For example, the information we reviewed that is given to TEC employees at the time they are hired and at annual staff meetings indicates that aides and program support staff (e.g., school secretaries) receive five paid vacation days and five paid sick days per year, whereas specialists, coordinators, program directors, and administrators receive up to 20 vacation days and 15 sick days annually. However, we found that in practice secretaries and other administrative support staff at TEC's central office receive 15 paid vacation days and 15 paid sick days per year. In addition, TEC senior managers are provided 30 paid vacation days rather than the 20 days shown on the handouts we reviewed.

Also, although TEC staff are advised in these handouts that unused leave time cannot be carried over from one year to the next, in practice, certain managers and central office administrative support staff have been permitted to carry over unused vacation days from one or more prior years. For example, at the start of fiscal year 2009, TEC's Executive Director allowed 14 employees to carry over a total of 131.5 unused paid vacation days, including 35 days for one administrator. Similarly, although the handouts provided to

employees do not reference paid holiday time, classroom aides and school support staff receive no paid holidays, whereas other staff positions receive 11 or 12 paid holidays and are also paid for additional days on which TEC offices are closed or operated on a limited staffing basis (e.g., Good Friday). This lack of formal personnel policies and procedures can result in benefits being provided to staff in an inconsistent and discriminatory manner. For example, we found that during fiscal year 2008, TEC's Executive Director awarded salary increases to certain employees beyond the annual raises authorized by TEC's Board of Directors. Specifically, during the spring of 2007, the Personnel Committee of TEC's Board of Directors approved compensation levels for each staff position, including an across-the-board 3% salary increase for managers and administrative employees effective July 1, 2007. However, on October 4, 2007, TEC's Executive Director, without any evidence of board approval, granted additional salary increases to seven selected administrative employees, as set forth in the table below.

Fiscal Year 2008 Retroactive Raises for Selected Employees

Position	Fiscal Year 2007 Salary	Board- Approved Fiscal Year 2008 Salary	Additional Retroactive Raise Amount	Revised Fiscal Year 2008 Salary	Cumulative Percentage Increase over Fiscal Year 2007 Salary
Network I Director	\$ 69,963	\$ 72,062	\$ 7,206	\$ 79,268	13.3%
Network II Director	67,925	69,963	6,996	76,959	13.3%
ABA Coordinator	80,000	82,400	3,600	86,000	7.5%
Purchasing and Payroll Coordinator	43,890	45,207	4,000	49,207	12.1%
Human Resources Coordinator	42,000	43,260	5,500	48,760	16.1%
Administrative Assistant (Main Office)	34,000	35,020	2,000	37,020	8.9%
Administrator of Finance and Operations	<u>80,000</u>	<u>82,400</u>	<u>4,000</u>	<u>86,400</u>	<u>8.0%</u>
Total	<u>\$ 417,778</u>	<u>\$ 430,312</u>	<u>\$ 33,302</u>	<u>\$ 463,614</u>	<u>11.0%</u>

The increases were made retroactive to July 1, 2007 and effectively provided actual pay increases of between 7.5% and 16.1% per employee rather than the 3% approved by the board. Further, these increases resulted in an additional salary expenditure of approximately \$33,302 plus associated tax/fringe benefit costs that had not been included in the budget approved by TEC member districts. In addition, the Executive Director approved special

cell-phone and transportation “stipend” payments to five managers totaling an additional \$7,320 for fiscal year 2008. Payment of those stipends was not linked to any underlying documentation that the employees had incurred actual expenses on behalf of TEC, and there was no documentation of board approval for the compensation. TEC’s Administrator of Finance and Operations defended the absence of formal policies and the variances from stated compensation and benefit arrangements by asserting that TEC managers needed “flexibility. However, the TEC collaborative agreement approved by TEC member districts and by the Department of Elementary and Secondary Education (DESE) prohibits such supplemental expenditures without specific approval by the Board of Directors. The agreement requires that TEC prepare and submit to each member town for approval a budget “showing in reasonable detail all expenses that may be required during that period to conduct each of the programs so proposed” and then states, “No funds received by TEC on account of this Agreement may be expended for any purpose or use not provided for by said budget unless such expenditure shall first have been approved by the Board.”

c. Significant Changes in TEC’s Retiree Health Insurance Benefits Could Result in Excessive and Unnecessary Costs to Collaborative Members

Prior to March 14, 2008, TEC required employees to work for the agency for at least 10 years in order to be eligible for TEC-sponsored health insurance coverage upon retirement, at which time TEC would pay 50% of the premium costs of their health insurance coverage. However, on March 14, 2008, TEC’s board eliminated the 10-year eligibility requirement. Under the revised eligibility criteria, no minimum length of employment at either TEC or other Massachusetts public employers is required. Rather, the new requirement is simply that “the eligible retiree must have been enrolled in the group health insurance plan of The Education Cooperative for at least one school year prior to the date of retirement and be an actively enrolled participant at the time of retirement.” TEC would then be responsible for paying 50% of the group health plan premium for the employee for the rest of their life or as long as the retiree elects to receive this benefit.

These changes carry obvious significant financial implications for TEC and its member districts. However, there was no documentation that cost projections had been developed or reviewed by TEC staff or its board to determine the financial impact of this change in benefit prior to its implementation. Further, we believe that this benefit is excessive when compared

to provisions at other Massachusetts public employers, which typically require that employees have worked at least 10 years at one or more governmental entities participating in either the Massachusetts teacher or public employee retirement systems.

d. Control over Taxable Compensation to the Executive Director and Certain Other Managers Was Deficient, Resulting in Tax Withholding and Reporting Deficiencies

In addition to the above-described \$635 per month health coverage payments to the Executive Director, he was provided with a \$2,000 per year travel allowance. However, TEC incorrectly treated this supplemental compensation as non-taxable until TEC's private accounting firm identified various tax withholding and reporting deficiencies. Similar reporting and withholding errors were made for the above referenced "stipend" compensation to five managers. When we discussed this matter with TEC management, we were told that they had decided to address the deficiency only "on a going-forward basis" starting July 1, 2008. As a result, only \$4,660 out of a total of \$16,940 in supplemental compensation had been properly reported and subjected to withholding for calendar year 2008. The balance of \$12,280 remained unreported, including \$8,620 paid to the Executive Director. TEC agreed to file corrective tax filings covering the unreported compensation for the first half of calendar year 2008 but stated that corrective filings would not be made for prior years where supplemental compensation had not been reported unless our audit included a recommendation that such retroactive corrective filings be made.

Recommendation

TEC should immediately develop and implement formal, written, board-approved personnel policies and procedures, including provisions relative to staff compensation and benefits. These policies and procedures should expressly prohibit compensation and benefits that are not within the parameters established by board-approved annual budgets and board-approved compensation and benefit schedules covering each position. Further, TEC should implement appropriate time and activity reporting and approval systems for all employees, not just hourly staff. Policies and employment contracts should also include detailed information and controls regarding any misuse of time and resources for private purposes and appropriate board approval requirements for outside consulting or other employment or business arrangements for senior managers. TEC should also rescind its policy change providing health coverage to retirees who have worked as little as one year at TEC. Benefits and policies should be consistent with those

established by member towns and other public employers in the Commonwealth, where the established norm is to require that employees work either for the employer or another public employer in the Commonwealth long enough to be vested in one of the Commonwealth's public employee retirement systems (typically 10 years). TEC should also file corrected taxable compensation filings with state and federal tax authorities for years prior to calendar year 2008 that are still within tax payment statute of limitation periods.

Auditee's Response

In response to the issues regarding potentially excessive and unallowable fringe benefits provided to TEC's Executive Director and inadequate controls over time and attendance, TEC officials stated, in part:

When the former Executive Director was hired in July 1, 2003, The TEC Board performed a nationwide search through New England School Development Council (NESDEC) to find a top-notch executive to grow the organization. The former Executive Director brought a wealth of experience with over 30 years as a Superintendent in both New York and Texas. He was paid according to his years of experience and his educational work with a Doctoral Degree in Administration. Typically, the executive directors of collaboratives have Master's Degrees and are Special Education Administrators; however, the TEC Board was looking for a higher-level educational leader and hired the former Executive Director and voted an appropriate salary level for him.

In Massachusetts, all public employees are eligible for health insurance and retirement benefits. Hence, the Executive Director did not receive any beneficial income from the State Retirement System or from TEC because he was already retired from another state and receiving health insurance benefits from that state. The Board of Directors agreed to reimburse him for membership in his retired out-of-state health insurance program. TEC's payments to the Executive Director were comparable to its payments for other employees within TEC. The board formally approved this reimbursement December 18, 2009.

TEC has revamped its vacation and sick leave documentation for the Executive Director position. In response to the notation regarding the Executive Director's secretary's calendar, it should be noted that the appointment book used is not an accurate summary of meetings or events. The purpose of the secretary's appointment book was to show who is physically in the building. It did not illustrate TEC related activities outside the office building. For example "out" in the appointment book meant the executive director was at a meeting for the day, at a TEC classroom, or at a training or at any other TEC related activity out of the building. The blank days in the appointment book would indicate days that the Executive Director spent in the office, meeting with staff and overseeing the day-to-day operation of TEC. These meetings would not be reflected in the appointment book. The calendar in the report was not the official calendar of the Executive Director or the staff but rather a personal calendar so that when calls came in, she would be aware if people were physically in or out of the building.

The TEC Board was fully aware that the former Executive Director was conducting Superintendent searches and was using his vacation time when needed for travel and

consulting. TEC is currently reviewing issues of time sheets, telephone calls, and vacation time reporting, to help improve our current system, in conjunction with revising the policy and procedure manual.

Auditor's Reply

We do not question that TEC's Executive Director was qualified to function in this position, and our report clearly acknowledges that most public employees in the Commonwealth are eligible to receive health insurance and retirement benefits. However, as stated in our report, we believe that some of the compensation provided to TEC's Executive Director during the period covered by our audit appeared to be excessive and contrary to the benefit levels approved by TEC's Board of Directors. For example, as noted in our report, the Board of Directors provided the Executive Director with an annuity to supplement his salary even though his salary already exceeded those of Executive Directors of larger education collaboratives in the Commonwealth and many Superintendents of TEC's member districts. We projected that cumulative annuity costs to TEC would total approximately \$71,111 at the time of the Executive Director's planned June 30, 2009 retirement. As stated in our report, the need to provide this additional retirement benefit to the Executive Director is also questionable, given that he was also receiving retirement benefits as the result of his past two retirements from Superintendent positions in Texas and New York State. We do not agree with TEC's assertion that the Executive Director did not receive any beneficial income from TEC from this supplemental annuity benefit. To the contrary, until such time as TEC's board approved his annuity supplement, the Executive Director was in fact receiving a benefit comparable to most other public employees within the Commonwealth. Specifically, a percentage of his compensation was being withheld and deposited into the appropriate state retirement fund. If the Executive Director chose to leave prior to the 10-year vesting period for this state retirement program, just like all other public employees, his total contributions to the fund would be returned to him. Similarly, if he chose to work and contribute to the retirement system for at least 10 years, which he had the option to do, he would have become vested in the retirement system and received a Massachusetts public employee pension. Consequently, the approximately \$71,000 in additional compensation TEC provided to the Executive Director through this supplemental retirement benefit, was clearly beyond the benefits provided to any TEC employee and most other public employees.

In its response, TEC states that its board formally approved the reimbursement for the Executive Director's health insurance premiums in December 18, 2009. However, as stated in our report, the Executive Director had authorized himself to receive these payments without formal board approval on August 14, 2003, retroactive to his first day of employment on July 1, 2003. The TEC board's retroactive approval of these payments over six years after the Executive Director authorized this benefit for himself is questionable and does not mitigate the fact that the Executive Director should not have received these benefits during the period in question, since they were not provided for by his employment contract or formally approved by TEC's board at that time. It should be noted that, even though the Executive Director's employment contract was amended multiple times after he initially authorized these benefits for himself, the original contract provision limiting his health benefit to the standard group coverage benefit provided to other TEC employees remained unchanged.

Since the Executive Director was not required to submit time sheets that documented his actual attendance at TEC, his appointment calendar, albeit an incomplete record, was given to us an official record of the Executive Director's schedule during the period in question. We acknowledge that this calendar may not constitute a complete record of the Executive Director's attendance. Nevertheless, as noted in our report, the information in this appointment calendar is concerning, given that certain of its entries clearly conflict with the time and attendance information maintained by TEC. For example, TEC's personnel and payroll records did not document the use of any leave time by the Executive Director during the period July 1, 2006 to February 28, 2009. However, the Executive Director's appointment calendar clearly indicates that he had taken at least 16 days of vacation during this period.

In its response, TEC asserts that the days on the Executive Director's appointment calendar marked "out" were in fact days on which the Executive Director was working at TEC but out of his office all day at meetings. However, as stated in our report, we found that during at least 9½ of the "out" days and five additional days where his appointment calendar had been left blank without reporting any absences or appointments, the Executive Director appeared to have been on location at consulting engagements in Virginia and Louisiana functioning as an employee for a private consulting company. Moreover, contrary to TEC's response that the board "was fully aware that the former Executive Director was conducting Superintendent searches and was using his vacation time when needed for travel and consulting," TEC's personnel and payroll

records indicated that no vacation time had been taken by the Executive Director. Moreover, clearly if TEC's board was aware that the Executive Director was engaged in outside employment, it should have established better controls over his activities to ensure that time spent working at TEC versus his private business was properly documented and authorized. Finally, TEC does not comment on the fact that the Executive Director's private consulting activity may have also involved the use of TEC telephones during workdays on which he was present at TEC.

TEC officials stated that, in addition to its board voting retroactively to approve benefits for the Executive Director, TEC "is currently reviewing issues of time sheets, telephone calls, and vacation time reporting." We believe such actions are necessary and again urge TEC to fully implement effective internal controls in these areas. For example, in addition to requiring appropriate time and activity reporting for senior managers, TEC should consider implementing specific employment contract and personnel policy provisions mandating disclosure and prior written approval of any outside employment by staff.

Auditee's Response

In response to the issue regarding the questionable compensation arrangements and raises provided to certain TEC staff and the absence of formal personnel policies and procedures, TEC officials stated, in part:

TEC is in the final stages of revising the personnel procedures manual and will be presenting it to the Board for review and acceptance at the March 2010 meeting. Issues of rollover vacation time and personal leave will be addressed. We are also updating our bylaws to reflect changes, and will present this information to the Board for a formal vote

.....

The Executive Director informed the Board of salary adjustments for staff members on October 4, 2007. The Executive Director provided certain administrative staff members with raises that exceeded the annual raises originally authorized by the Board of Directors. These raises were provided as a result of a survey done in our districts that found that salaries of TEC administrators had fallen far behind those of comparable positions in our districts. Adjustments were nominal and although the percentage increase would look notable, the actual dollar amounts were not excessive given market conditions, which were analyzed prior to the adjustment. The Board was informed of these raises but a vote was not recorded. A vote has been taken and accepted by the Board on December 18, 2009. Future salary adjustments will first be submitted to the Board of Directors for approval by vote prior to implementation.

Auditor's Reply

In its response, TEC asserts that it is in the process of revising its policies, procedures and bylaws. We believe that such actions are necessary and appropriate, but urge TEC to expedite this process, since TEC has been in the process of updating certain agency policies and procedures since 2007.

TEC further asserts in its response that its Executive Director “informed the Board of salary adjustments for staff members on October 4, 2007” and that the board “was informed of these raises but a vote was not recorded.” However, we were not provided with any documentation that indicated that the board was informed of the pay raises in question prior to their implementation. In fact, the first meeting of TEC’s Board of Directors for the 2007/2008 school year was not held until October 12, 2007 -- eight days after the Executive Director sent a memorandum to TEC’s Administrator of Finance and Operations to implement these raises. Neither TEC’s board nor TEC’s Treasurer were listed as recipients on the aforementioned memorandum, and no reference was made to the raises being contingent on subsequent approval by TEC’s board. Further, according to the minutes of TEC’s October 12, 2007 board meeting, the Executive Director provided a detailed personnel update on new hires and sought and obtained approval for benefit plan changes required for compliance with Massachusetts health care reform. However, the minutes do not reference the salary increases in question.

In its response, TEC asserts that the “raises were provided as a result of a survey done in our districts that found that salaries of TEC administrators had fallen far behind those of comparable positions in our districts. Adjustments were nominal and although the percentage increase would look notable, the actual dollar amounts were not excessive given market conditions, which were analyzed prior to the adjustment.” However, we found that the survey TEC references in its response was not prepared until late April 2008, over six months after the raises in question had been implemented. Consequently, we question the extent to which information in this survey could have been available to be used as a basis for the pay raises in question. Clearly, the TEC board’s retroactive approval of these pay increases over two and one half years after they were originally provided does not mitigate that the Executive Director did not get the required approval for these pay increases at the time they were provided. The point that TEC makes in its response that the total additional compensation provided to these individuals under these pay raises was not significant is not the issue. Rather, our concern is that

the process followed by TEC's Executive Director in providing these pay increases was clearly not consistent with the requirements for such expenses in TEC's collaborative agreement.

Auditee's Response

In response to the issue regarding the changes made by TEC to its retiree health plan benefit, TEC officials stated, in part:

The TEC Board voted to change the 10-year requirement for TEC employees in order to be eligible to receive health insurance upon retirement. TEC is aligned with our districts and all other government agencies. All employees must still have at least 10 years in the retirement system and also be eligible for retirement under state standards to receive these health benefits. All of the districts that belong to TEC follow the requirements of Massachusetts General Laws, Chapter 32, which applies to all municipalities. If one retires under the Massachusetts State Law under any state or local jurisdiction you are entitled to health payments from the last place at which you were employed even if you had only been employed for a short time period. This change recognizes and confirms state law and practices by the Commonwealth, all agencies of the Commonwealth and all subdivisions including cities and towns. A survey of TEC member communities finds that they do not have a 10-year pre-condition for eligibility of health insurance benefits. Highly qualified candidates have been reluctant to join TEC because of this former policy. In addition, TEC's contribution level of 50% is less than the 75%-80% employer contribution level in most communities and for the Commonwealth.

Auditor's Reply

In its response, TEC states, "TEC is aligned with our districts and all other government agencies. All employees must still have at least 10 years in the retirement system and also be eligible for retirement under state standards to receive these health benefits." However, unless TEC has further amended the policy language approved by its Board of Directors on March 14, 2008, this assertion is in conflict with the documentation relative to this benefit approved by TEC's Board of Directors and provided to us during the conduct of our audit field work. Specifically, the minutes of the TEC board meeting on this date state that TEC eliminated the 10-year length of service retiree health coverage eligibility requirement at that time. Under the language adopted by the board at that meeting, retirees are not required to have worked at least 10 years total at either TEC or at another public employer in the Commonwealth's retirement system. Instead, the language only requires that "the eligible retiree must have been enrolled in the group health insurance plan for at least one school year prior to the date of retirement and be an actively enrolled participant at the time of retirement." Previously, TEC had required the eligible retiree to work at least 10 years at TEC, without counting any prior work at other public employers in the Commonwealth's retirement system. Although the prior policy was, in fact,

more restrictive than was typical, the revised policy is far more permissive than policies in place at other Massachusetts public employers. As stated in our report, there was no documentation that cost projections had been developed or reviewed by TEC staff or its board to determine the financial impact of the benefit change and, in our opinion, the revised benefit is excessive compared to benefits provided by other public employers. If it was not TEC's intent to eliminate the 10-year length of service requirement but rather to simply allow credit in situations where a portion of the 10-year period had been served through employment at another Massachusetts collaborative, school district, or other public employer, TEC should have phrased the policy language differently.

Auditee's Response

In response to the issue of TEC's not properly withholding taxes or reporting taxable income to certain individuals during our audit period, agency officials stated, in part:

The independent certified public accountant provided a management comment that indicated certain payments should have been included on a W-2. The organization had been reporting the income to the IRS through the miscellaneous income box located on IRS forms 1099. When notified that this procedure should be changed, the organization took immediate steps to do so. Additionally, for prior years when the classification error occurred, the organization indicated that it would obtain expert advice for retroactive treatment once it had received all of the recommendations from the state auditor's report. It is important to note that the independent auditor's report prepared by certified public accountants did not note any material weaknesses in the internal control structure of TEC. Moreover, the reports issued "unqualified" opinions on the fair representation of the financial statements prepared by managementThe stipends to five managers were reported to the Internal Revenue Service through the IRS Form 1099 process. The procedure has changed to report stipends on the employee's W-2.

Auditor's Reply

Our report acknowledges that, after this problem was identified by auditors from TEC's private accounting firm, TEC took some measures to withhold taxes and report the taxable compensation in question on a going-forward basis. However, since TEC had only started withholding and reporting the additional compensation in question as taxable for the second half of calendar year 2008, the tax filings prepared by TEC for the entire calendar year remained inaccurate. In addition, we determined that withholding and tax filings for prior tax years were also in error. As a result, as of the end of our audit fieldwork, a total of \$12,280 in taxable compensation remained unreported for calendar year 2008, including \$8,620 paid to the Executive Director. The fact that TEC's private accounting firm had not reported material

internal control deficiencies during its audits in this area is not relevant to this issue. Although TEC's accounting firm did not identify this issue as a material internal control deficiency, it was formally disclosed in a management letter to TEC by its accounting firm as an issue that should be addressed. Even though the amounts of unreported compensation in question did not have a material impact on TEC's financial statements, it does not mitigate TEC's responsibility to ensure that it withholds correct tax amounts and files accurate tax reporting documents.

2. BUDGETING, ACCOUNTING, AND PROGRAM SERVICE PRICING DEFICIENCIES RESULTED IN INSUFFICIENT INFORMATION BEING PROVIDED TO TEC'S BOARD TO EFFECT PROPER OVERSIGHT AND QUESTIONABLE SURPLUSES IN EXCESS OF \$1.4 MILLION

As a local governmental entity, TEC is required to establish systems that allow it to accurately budget and monitor its revenues and expenses and to develop detailed budget estimates so that it can establish accurate prices or fees for its program services. Accurate budget estimates and comparisons of budget to actual revenue and expense information are also essential for board oversight purposes. The Massachusetts Department of Revenue's Division of Local Services (DLS) and the state's Office of the Attorney General (OAG) have issued guidance relative to the amount of fees governmental agencies such as TEC can charge for their services. This guidance effectively states that the amount of fees a governmental agency should charge for services should not exceed its actual cost of providing the services. However, we found that TEC's budgeting, financial reporting, accounting, and pricing systems do not allow TEC's board to effect proper oversight of the agency and ensure proper accountability. Further, due to its inadequate accounting and budgetary controls, TEC has charged excessive fees to its member and non-member school districts, resulting in TEC's accumulating, over a multi-year period, a total of \$1,465,139 in total net assets (profits) of as of June 30, 2008, which is inconsistent with DLS and OAG guidance.

Municipal government agencies in Massachusetts have been advised on different occasions by DLS and the OAG that service fees may be used to offset the costs of providing services but may not be used to produce a surplus or profit in excess of the costs of the program, since to do so would constitute a constitutionally prohibited exaction. For example, on December 24, 2003, the then Massachusetts Attorney General responded to an inquiry from the Town Clerk of Bridgewater regarding the implementation of a fee by the town by stating, in part:

In approving the fees established in Article XXXVIII, we remind the town that fees cannot exceed the limits imposed on local government by the Constitution and the statutes of the Commonwealth. Valid fees are distinguishable from invalid taxes by three criteria: (i) the fee is assessed for a particular government service benefiting the party paying the fee in a manner not shared by other persons; (ii) the person assessed has the option to decline the service and thus avoid the charge; and (iii) the amounts paid compensate the town for its costs and expenses of providing the services rather than raising revenues. Emerson College v. Boston, 391 Mass. 415, 427-28 (1984). Moreover, a lawful fee is one that covers only the permit granting authority's reasonably anticipated costs of providing the services for which the fee is assessed. Southview Cooperative Housing Corp. v. Rent Control Board of Cambridge, 396 Mass. 395, 402 (1985)

Similar guidance has also been promulgated by the Commonwealth's Executive Office for Administration and Finance (EOAF) for use by state agencies. Specifically, EOAF Bulletin No. 6 states, in part:

Fees may not be used purely as a tool to raise revenue, but should reflect the government's expense in providing the service associated with the fee. Expenses may be defined as the reasonable costs imposed on an agency for providing a service or regulating an activity, including administrative and enforcement costs.

In order to ensure that their established prices or fees are consistent with the aforementioned guidance, entities such as TEC must ensure that they utilize effective budgeting and cost accounting practices to establish their fees. However, we found that TEC's budgeting, cost accounting, and pricing systems are not effective in ensuring either the proper oversight by TEC's management and board or the proper pricing of program services. The specific issues we found in each of these areas are detailed below:

Budgeting Deficiencies

As previously discussed, TEC's collaborative agreement requires preparation and approval of a collaborative "showing in reasonable detail all expenses that may be required during that period to conduct each of the programs so proposed" and prohibits the expenditure of funds "for any purpose or use not provided for by said budget unless such expenditure shall first have been approved by the Board." However, during our audit, we found that TEC's administrative staff routinely prepared and obtained approval of only a partial budget from TEC's board. The table below summarizes the major costs we identified that were not included in the budgets approved by TEC's board for the fiscal years ended June 30, 2007 and June 30, 2008.

Summary of Budgeted and Unbudgeted Expenses

	Fiscal Year 2007	Fiscal Year 2008
Total Budgeted Expenses	\$5,772,036	\$6,613,844
Total Actual Expenses for Budgeted Activity Reporting Centers	\$5,731,128	\$6,330,824
Total "Off-Budget" Unbudgeted Expenses	\$783,180	\$386,361

The expense items not included in these budgets, or what is referred to as off-budget expense reporting centers shown in the table, include a variety of activities such as grant programs, programs operated on a special basis for one purchasing school district, regular programs serving multiple purchasers, and legislative agent services. Although each year the budget included modest provisions for unspecified "Miscellaneous Programs" (\$25,966 for fiscal year 2007 and \$44,264 for fiscal year 2008), off-budget activities far exceeded these budget provisions for miscellaneous programs. For example, for fiscal year 2008 we identified eight off-budget activity reporting centers, which included a federal Teaching American History Grant, three other grants, "government consult" expenditures for legislative agent and related services, a small transportation contract program for one school district, and the Elementary Teacher Licensure and Medfield Summer programs. TEC's Administrator of Finance and Operations confirmed that expenditures totaling \$386,361 during this fiscal year for those activities had not been included in the budgets approved by TEC's Board of Directors.

We also found that even though the TEC Board of Directors routinely approves budget revisions at approximately the midpoint of each fiscal year, significant variances between budgeted and actual revenues and expenditures exist at year-end. This is because TEC's expenditure controls are inadequate in that they allow substantial expenditures of amounts not approved by the board either in the budget or by special approval as required by the TEC collaborative agreement. Budget revenue projections have also been consistently inaccurate, with actual revenues significantly exceeding budgeted amounts. The table below illustrates the variances in budgeted versus actual expenses incurred by TEC during fiscal year 2008.

Budgeted Versus Actual Expenses
Fiscal Year 2008

	Original Budget	Revised Budget	Actual from General Ledger *	Excess of Actual over Revised Budget
Consolidated Core and Business Administrative Expenses	\$ 1,007,512	\$1,318,662	\$ 1,229,591	\$ (89,071)
Allocated to Programs	<u>(399,375)</u>	<u>(489,855)</u>	<u>(399,375)</u>	<u>90,480</u>
Unallocated Administrative Expenses	\$ 608,137	\$ 828,807	\$ 830,216	\$ 1,409
Expenses for Budgeted Program Activity Reporting Centers	<u>5,206,095</u>	<u>5,785,037</u>	<u>5,500,608</u>	<u>(284,429)</u>
Expenses for All Budgeted Activity Reporting Centers	\$5,814,232	\$6,613,844	\$6,330,824	\$ (283,020)
Expenses for Off-Budget Reporting Centers	<u>-</u>	<u>-</u>	<u>386,361</u>	<u>386,361</u>
Total Expenses	\$ 5,814,232	\$ 6,613,844	\$ 6,717,185	\$ 103,341
Total Revenue	<u>\$ 5,814,232</u>	<u>\$ 6,613,844</u>	<u>\$ 7,119,052</u>	<u>\$ 505,208</u>
Excess of Revenue over Expenses	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 401,867</u>	<u>\$ 401,867</u>

* The actual revenue and expense amounts shown in the above table were derived from TEC's accounting records prior to year-end adjusting entries. After adjustment, the audited financial statements reported a net operating surplus of \$307,594 and \$35,935 in proceeds from a capital lease, for a total increase of \$343,529 to the TEC Governmental Funds fund balance. Coupled with other changes involving the TEC Non-Major Governmental Fund, the overall result was a \$309,848 increase in TEC's Total Net Assets account balance.

Each year TEC managers present the Board of Directors with what is represented to be a balanced "break-even" budget, with budgeted revenues equal to budgeted expenses. However, our audit found that each year TEC's budgets have significantly underestimated its revenues and have not included all organizational activities and expenditures. At the same time, as evidenced by the information in the above table, budgeted expenses have generally been overstated for the activities that have been included in the budget. As a result, budgeted-to-actual comparisons for individual budgeted direct service programs reveal wide variances by program. For example, during fiscal year 2008, TEC's Professional Development program overspent its budget by 53%, whereas the Intensive I network school year program underspent its budgeted amount by 11.9%. Overall, most programs underspent their budgets, resulting in the net \$284,429 (4.9%)

underspending shown in the above table. These budgeting practices effectively undermine the control function ordinarily associated with use of an approved organizational budget and have resulted in TEC member districts and other governmental purchasers of TEC services being charged more than is reasonably necessary to perform services on their behalf.

Accounting Deficiencies

TEC revenues are derived from multiple sources, including annual member charges, tuition payments from member and non-member districts, additional charges to districts for services provided to students on an hourly fee basis, professional development fees paid by either districts or individual educators, grant revenues, and miscellaneous revenues such as meal receipts for culinary arts classes at the TEC Phoenix School program. We found that TEC's revenues and expenses are not always appropriately charged to accounting functional activity centers and are sometimes charged differently than as presented in TEC's budgets. We also noted that matching revenues and expenditures are not accurately presented for each functional activity, and indirect costs and offsetting revenues are not accurately presented and allocated to activities on a reasonable basis.

For example, even though a separate activity reporting center ("Business Administration" services) has been established in TEC's general ledger for Cooperative Purchasing services, only limited expenses such as bid advertising costs are recorded there. Significant personnel, occupancy, photocopying, and other costs associated with carrying out the services are instead incorrectly recorded as costs for the "Core" Administration/Management and General activity center in the general ledger, and no allocation of indirect administrative costs is made to the program reporting center. However, all revenues associated with the program are credited to it in TEC's general ledger. As a result, TEC's general ledger for fiscal year 2008 reported \$59,523 in revenue for this program but only \$6,031 in expenses. We found similar budgeting and reporting deficiencies for most of TEC's activity centers.

In addition, costs and revenues were not always budgeted or reported on a consistent basis from year to year, and expenses or revenues for a particular activity were frequently moved from one reporting center to another or were reported under different revenue or expense classification lines. For example, \$2,148 expended for a holiday party in fiscal year 2007 was classified as "special program expense," whereas \$1,195 expended for the holiday party in fiscal year 2008

was classified as “meeting expense.” An example of inconsistencies in the budgeting and reporting of revenue involves “program income,” which is included in the board-approved budget each year as a discrete type of income separate from other income classifications such as tuition income, registration income, and interest income. For fiscal year 2007, program income was originally budgeted at \$199,700, all of which was identified as direct income to the Core Administration/Management and General activity center. When the budget was revised, the anticipated revenue amount for this item was reduced to \$164,634, without any explanation for the adjustment. However, at year-end, actual program income reported in the general ledger for this activity totaled only \$300 – all of which was reported as revenue for the Professional Development activity-reporting center, with no program income whatsoever reported for the Core Administration/Management and General activity center. At the same time, TEC operated Administrator Licensure and Teacher Licensure programs for the purpose of providing training and experience needed by teachers and educational administrators to obtain or upgrade DESE professional licenses. Activity reporting centers had been established in the general ledger for both programs. However, these reporting centers were omitted from the board-approved budget, which identified neither licensure program expenditures nor revenues that year. Yet the general ledger reported a combined total of \$312,125 in “licensure income” for those two programs, plus additional licensure income in four other activity reporting centers, for a total of \$323,970 in licensure income for fiscal year 2007, none of which had been identified in either the original or revised budgets of TEC.

In providing program services, entities such as TEC 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 but are still necessary for the overall operation of the entity, they need to be allocated to each of an entity’s activities using an acceptable cost allocation method. This allocation process is necessary to ensure that all costs are appropriately recognized when budgeting activities and establishing program prices. Otherwise, the true costs of carrying out an activity will not be recognized. However, during our audit, we found that TEC allocated its indirect costs in an essentially arbitrary manner in different amounts to some but not all of its functional activity reporting centers. Additionally, TEC typically allocated only a portion of its total overhead expenses out to those centers. For example, as summarized in the previous Budgeted Versus Actual Expenses table for fiscal year 2008, only a fraction of TEC’s

indirect costs had actually been charged or allocated to direct activity reporting centers, while approximately \$830,000 remained unallocated. As a result, the actual true costs associated with various TEC activity centers were not calculated or made available to managers, the TEC Board of Directors, member school districts, or other parties in need of this information.

Moreover, although multiple reasonable allocation methodologies might be used for the purpose of allocating indirect costs to activity reporting centers, we noted that TEC's allocations did not adhere to any standard accepted methodological approaches. Our analysis performed for fiscal year 2008 indicated that indirect allocations established by TEC managers varied from the results of acceptable methodologies by \$20,000 or more for at least seven reporting centers and that, in some instances, variances were as high as \$98,000 for individual programs such as Network I classroom services for students with mild to moderate disabilities. For 12 reporting centers (including two of the above seven) TEC managers had made no indirect allocations whatsoever.¹ As a result, it is likely that the net operating results reported by TEC for its various program activities vary significantly from results that would be reported had a reasonable accepted indirect cost allocation methodology been used. For example, TEC reported \$140,401 in direct expenditures for its Middle Therapeutic program with no additional indirect costs allocated. Revenue was reported as \$141,089, with a resulting net excess of \$688 in revenue over expense. However, had an appropriate allocation of indirect costs been made to the program, the program might in fact have been more accurately reported as having lost over \$20,000 in fiscal year 2008. In other instances, indirect allocations assigned by TEC managers, such as a \$5,500 allocation to a contracted transportation program with only \$7,574 in direct expenses, appeared to be excessive.

In order to ensure that oversight systems work as intended for governmental entities, including education collaboratives such as TEC, it is essential that all operations be properly defined and budgeted and that actual revenue and expenditures be accounted for and reported in a manner that permits meaningful comparison of budget to actual results. When significant activity areas, as discussed above, are excluded from the budget or revenues and expenditures are not

¹ For the purpose of this discussion, certain activity reporting centers used in the TEC general ledger have been consolidated to conform to the budget's presentation of reporting centers. For example, the approved budget uses two reporting centers each for the Network I classroom programs. One center is for a Network I Summer program and another covers the consolidated Network I school year activities for multiple classrooms located in multiple communities. In actuality, the general ledger has separate reporting centers for the summer program and for each classroom. The count presented here consolidates those classroom reporting centers in the manner used by the budget.

accurately reported, the resulting budget-to-actual comparison presentations can be misleading, and accountability is impaired. In our opinion, the budgeting and accounting deficiencies we identified have distorted the presentation of budget-to-actual comparisons appearing in TEC financial statements and have adversely affected TEC's accountability to its Board of Directors, member school districts, and the public.

Pricing Deficiencies

The deficiencies discussed above in TEC's budgeting and cost accounting practices, in our opinion, makes it impossible for TEC to establish fair and reasonable charges for its services in compliance with DLS and OAG guidelines. As noted in the Background section of this report, TEC generates revenues through assessments paid by member school districts, tuition charges, and other service fees paid by both member and non-member districts and, in some cases, by educators and parents. In addition, miscellaneous income is provided by grants, contracts, and contributions from state, federal, local government, and private sources and from interest income generated by bank accounts and investments. TEC's member assessments, which totaled \$342,100 for fiscal year 2009, are established by TEC's board and are calculated on a formula whereby half of the voted assessment total is charged to members on an equal pro-rated basis, while the remaining 50% is charged to each member in proportion to student enrollment. As a result, member assessments for individual districts vary from approximately \$19,000 to over \$38,000. However, these assessments are not designed to cover the full cost of providing services to members, and members are also charged additional program-specific service fees. Since non-members are also allowed to purchase TEC services without paying member assessments, the TEC bylaws authorize the use of higher fees for non-members, stating:

TEC may sell materials and services to non-member towns to help underwrite the cost of material production or the provision of services. Tuition programs that are opened to non-TEC students will be charged at a per pupil direct service cost plus a 12% surcharge for administrative overhead.

TEC's prices for its services would comply with DLS and OAG guidelines if the combination of member assessments and service fees paid by member districts covered TEC's actual direct and indirect costs incurred in servicing member districts and the surcharge-based fees to non-members covered the actual direct and indirect costs incurred in providing services to non-members. However, when we discussed pricing methodologies and issues with TEC officials, they stated that TEC's pricing approach was "entrepreneurial" and that, rather than setting

prices on the basis of anticipated actual costs, prices had been set to compete favorably with private special education school rates and that school districts that were not TEC members were charged higher rates to effectively subsidize services to TEC members. In fact, TEC's Executive Director stated that one non-member school district (Millis), which had been purchasing services as a non-member, wished to join the collaborative but that it was not in the interests of the TEC member districts to admit the new district since they were currently making a profit from services to that district.

During our audit, we analyzed TEC's fiscal year 2008 prices for nine services and confirmed the existence of wide variances in prices charged to both member and non-member districts. The results pointed to an irrational pricing system whereby the charges for at least two of the services (the TEC Learning Disabilities "Academy" program and the TEC Therapeutic Early Elementary program) to both member and non-member districts were not sufficient to cover the programs' budgeted operating costs. For three services (TEC Intensive II Network services, Phoenix Middle School, and TEC Therapeutic Middle School), members were charged below calculated budgeted costs while non-members were charged in excess of budgeted unit costs. For the remaining four services (TEC Intensive I Network, Phoenix High School, TEC High School, and the TEC Therapeutic Elementary program) both TEC member and non-member districts were charged in excess of budgeted costs. Rates charged to non-members were also from 15% to 76% higher² than rates charged to members despite the provision of the bylaws requiring use of a flat 12% surcharge. All four of the services for which both member and non-member rates exceeded budgeted unit costs generated surpluses, and two of those generated revenue substantially in excess of reported expense. The Intensive I Network generated \$349,374 in excess revenues over expenses (24.2%), and the Phoenix High School generated \$258,601 in excess revenues over expenses (45.3%). Together with \$173,785 in apparent surpluses derived from Professional Development services, these activity centers effectively cross-subsidized other program and administrative activities and accounted for the TEC's substantial increase in net assets that year.

In order to comply with DLS pricing guidance, TEC should have adjusted its bylaw non-member fee surcharge provisions to reflect actual indirect administrative cost rates net of member assessments and other offsetting support and maintained appropriate budget, cost

² Most rate differences were 20% or 25%.

accounting, and cost allocation systems needed to calculate service fees in compliance with state requirements. Alternatively, TEC could have simplified its pricing methodology by eliminating member assessments and simply establishing legally compliant uniform fees to be charged to both members and non-members for each service provided. In either case, TEC's practice of using fees to generate profits for government services is not consistent with DLS and OAG guidelines.

As a result of these questionable pricing arrangements, by the end of fiscal year 2008, TEC had accumulated a total net asset balance of \$1,465,139. It is important to note that as of July 1, 2003, when the Executive Director began working at TEC, the agency's reported net assets totaled only \$412,586 and that during the prior year TEC essentially broke even, with a small loss of \$12,166. However, during the following five years, TEC generated over \$1 million in excess revenues over expenses. TEC's Administrator of Finance and Operations defended the generation of these substantial accumulated net assets, noting that they only represented the equivalent of approximately two months of operating costs, which in her opinion was prudent for cash flow and cash reserve purposes. However, it should be noted that Chapter 40, Section 4E, of the General Laws allows school districts to pay collaboratives in advance of service delivery. As a result, education collaboratives are not in a situation similar to other organizations that must incur significant service delivery costs before they can bill for services and take in revenue. We also noted that at 2008 fiscal year end, TEC held \$1,230,003 in cash and cash equivalents but reported total current liabilities of only \$422,291. In any event, the rationale provided by TEC management would still not justify continuation of TEC's pricing arrangements given the contravening legal guidance issued by the state.

Recommendation

TEC should take measures to ensure that its budgeting, cost accounting, and service pricing activities are consistent with DLS guidance as well as the provisions of TEC's Collaborative Agreement and bylaws. This would involve developing:

- Appropriate budgeting, cost accounting, and pricing measures consistent with requirements of the TEC collaborative agreement and applicable guidance for local governmental entities on cost accounting practices and permissible fee levels; and
- Expenditure controls ensuring that all expenditures are adequately documented and approved by the TEC Board of Directors either through budget approval, or

by documented board authorization as required by the TEC collaborative agreement.

TEC should also take action in consultation with DLS, DESE, and the OAG to return excessive fee revenues to purchasers should those oversight agencies determine that such action is warranted.

Auditee's Response

In response to this issue, TEC officials stated, in part:

It should be noted that the surplus of \$1.4 million noted in the report is unusually high for this organization. However, use of our services by special needs students and others can be sporadic. That is, many students may move out of these programs at midyear, lowering revenues to TEC and resulting in the programs running a net loss over the fiscal year. The revenues of educational collaboratives are based heavily on tuitions. We closed last year with a loss of \$330,000, which reduces the fund balance by that amount. In FY2010, we are facing a shortfall of \$400,000, which again will bring the fund balance to about \$700,000, or about half of what the end of FY08 showed.

The variables of students moving in and out of TEC programs can result in both high and low fund balances based on circumstances not known when rates are set approximately 18 months before the end of the fiscal year. Without this tuition-setting method, collaborative organizations will be in danger of going out of business across the state and the result will be that private schools will have a monopoly on special education and communities will be paying millions more in special education costs. TEC surveys and does a comparative analysis of our programs and private placements, and presents this information to the Board of Directors.

Budgeted Programs vs. Unbudgeted Programs

The budget will be presented consistent with the TEC Agreement on actions necessary after the budget is set. The Board of Directors will be asked to approve or disapprove as they see fit.

Budgets are prepared on a break-even format. The organization's sources of revenue are highly unpredictable because of the nature of the majority of collaborative programs. In fact, roughly 80% of its revenue is derived from its special education programs in moderately intensive, severely intensive, therapeutic programs, and alternative programs. All of these programs have as a main mission the objective of servicing youngsters aged 3-22 in an inclusive setting where the goal is to return the student to the sending school. In other words, TEC actively seeks to minimize income to the collaborative because it is in the best interests of the student and the sending school district.

There are anticipated wide variances in the budget due to activity changes. TEC does not know from year to year how many students will attend each program, whether there will be need for new programs, or even if the majority of its classrooms will be available to it, thereby forcing TEC to move classrooms from town to town. One of the great attributes of TEC is its ability to adapt programs to meet the needs of the member and non-

member towns. In some years the organization will earn a surplus, and in other years, such as in FY09, TEC will need the money to offset its costs.

Accounting Deficiencies

As in any organization, there will be minor inconsistencies that surface in classification of expenses and revenues but there have not been material misstatements as evidenced by the clean opinions that TEC received in its audits by independent certified public accountants. For the Business Administration services for Cooperative Purchasing, the expenses were not segregated from the CORE sub-account because it was inefficient to do so. All of the costs associated with the Business Administration program had been identified in the CORE account and it did not make sense to carve those expenses out but rather did make sense to merge them with the CORE administration account. TEC will review that decision and determine if there should be a change. In the case of the "holiday party", there had been changes in administrative staff and the determination to change the expense classification was not to create a subterfuge but rather to add it to a category, which, because of materiality, was likely to be looked at by the independent certified public accountants.

Program income was a category that reflected "transfers" of "profit" from various programs to balance the budget. However, when transferring the "profit," the decision was made that it appeared to skew results of the programs so that a reader could not identify what were the operational results of each program from year to year. Once again, the decision made was to clarify not cloud the results of operations. The TEC management will take the comment under advisement.

The licensure reporting centers were included in later budgets when staffing changes resulted in different decisions being made, all for the purpose of presenting the readers with as much disclosure as possible.

Indirect costs in FY08 were allocated on the fairest basis possible, which was equitably based on expected expenditures. Each of the programs incurred approximately 10% in overhead, which was more than a fair charge for each program. The goal was to earn enough program income, assessments, and other income to cover the remaining \$830,000 of CORE costs. However, additional CORE expenses could have been allocated out equitably, which merely would have resulted in higher overhead charges per program.

Once again, the organization is unable to depend on "appropriations" sufficient to cover a budget since it is not a municipality. There is nothing that has been written into Massachusetts General Laws that indicates that collaboratives are subject to DLS and OAG in the same fashion as a municipality

The fact that the Executive Director indicated that TEC was increasing its fund balance to meet future unforeseen obligations is a point that should be commended. TEC must function independently, and it would not be appropriate for the organization to run deficits. The Executive Director's comment regarding Millis was misunderstood. The Executive Director was citing an example of any town joining TEC and the organization not wanting to become too large. In fact, Millis has been welcomed into the organization beginning September 1, 2009.

The fact that charges for certain programs were insufficient to cover the costs highlights the philosophy that TEC has utilized to subsidize proceeds of some programs for the benefit of all of the members and to offer a complete continuum of special education

services. Although the bylaws stipulate a certain pricing structure, they are over 30 years old and are currently under revision.

The state auditor's report concluded that because Massachusetts General Laws allow school districts to pay collaboratives in advance of delivery of service, they can bill for services and take in revenue. In fact, many towns do not pre-pay for services; they dispute bills and refuse to pay some bills. Additionally, in years past, there had been times that TEC had overdrawn its operating balance or had to rely on line of credit advances (for which significant interest charges had been incurred). Moreover, without adequate net assets, the organization would be unable to secure a line of credit should it ever need it in the face of the poor economy, 9C cuts, and reductions in enrollment.

Controls are in place for expenditures.

As previously stated, the organization had been in operation as a 501 c 3 organization approved by the IRS, and rules for not-for-profits are different than those for Massachusetts municipalities. Notwithstanding, the organization, as part of its operations, generally provides lunches to participants of job-alikes where business and innovation are regularly discussed on a monthly basis. We recognize that we are a government entity and as such, some rules have changed regarding our organization. The auditors' report pointed out that there are ambiguities in laws governing collaboratives'. We are including correspondence ... from the Department of Revenue that indicates that they are unable to advise us as to whether education collaboratives are further restricted by Massachusetts General Laws beyond Chapter 40 Sec. 4E

Items like federal grants do not require a separate approval by the Board to expend funds. The act to accept the grant carries with it the authorization to expend the funds without further authorization. This is true in the state and every city and town in Massachusetts. The Board voted on December 18, 2009 to accept grant funds previously received. In the future, the Board will be voting to accept the funds and authorizing the treasurer to expend the funds without further appropriation

We are sending the issue of tuition rates to our attorney for his review. However, preliminary but not official response from the Department of Revenue is that school tuitions are not included in the Emerson case decision. Cooperative member towns are free to choose any vendor for these services. TEC communities saved hundreds of thousands of dollars in special education costs by using TEC-provided services. Charging a higher fee for non-TEC members is very fair and appropriate, as those who are not members do not pay an annual assessment as TEC communities do. In addition, it is standard practice in regional schools across the state to charge higher tuitions to school systems outside of the regional authority.

Auditor's Reply

As detailed in our report, we found a number of issues within TEC's budgeting and accounting process that affect its ability to accurately budget and monitor its revenue and expenses and to establish accurate prices or fees for its program services. We do not agree with TEC's assertion that it and other education collaboratives need to price program services in a manner likely to generate surpluses in order to avoid going out of business. To the contrary, sound budgeting, accounting, and program pricing methodologies will further ensure the fiscal health of any

organization, including education collaboratives such as TEC, and further ensure that TEC's members and other school districts are charged fair but not excessive prices for program services.

We acknowledge that fund balances at TEC and other education collaboratives may vary depending upon the results of operations during any fiscal year. We also recognize that, given the nature of the special education and other services that TEC and other collaboratives provide, there will be variances between actual and budgeted costs and revenues. The fact that such variances can arise, and the potential for the resulting adverse consequences is a fundamental reason why it is essential for organizations such as TEC to employ effective budgetary controls. As detailed above, DESE-approved provisions in the TEC collaborative agreement require that a budget be prepared "showing in reasonable detail all expenses that may be required during the period to conduct each of the programs so proposed" and that expenditures not be made "for any purpose or use not provided for by said budget unless such expenditure shall first have been approved by the board." Those requirements are appropriate and consistent with the principles of effective budgetary control; however, as documented in our report, TEC did not always adhere to those requirements during the period covered by our audit. Rather, we found that TEC's administrative staff routinely prepared and obtained board approval for only a partial budget that omitted hundreds of thousands of dollars in anticipated costs and revenues. Although the budgets submitted to the TEC board for approval were, as stated in TEC's response, "balanced," the budgets varied significantly from TEC's historical revenue and expense data and were therefore not as useful as they could be both for administrative control purposes and for providing TEC's Board of Directors with meaningful information for oversight and planning purposes.

In its response, TEC states that it does not believe it is necessary to include some of the items in question such as grants in the budgets that it submits to its board and asserts that items "like federal grants do not require separate approval by the Board to expend funds. The act to accept the grant carries the authorization to expend the funds without further authorization. This is true in the state and every city and town in Massachusetts." However, we believe that this assertion is not consistent with the terms and conditions of TEC's own collaborative agreement. It is clearly in the best interest of TEC to fully disclose all anticipated revenues and expenses to its board through its budget development and approval process so that the board can properly

effect appropriate oversight of TEC's activities. We also found that even though TEC's board routinely approves budget revisions at approximately the midpoint of each fiscal year, significant variances between budgeted and actual revenues and expenditures exist at year-end because TEC's expenditure controls are inadequate in that they allow substantial expenditures of amounts not approved by the board either in the budget or by special approval as required by the TEC collaborative agreement. Further, TEC's budgets have significantly underestimated its revenues and have not included all organizational activities and expenditures. As a result, budgeted-to-actual comparisons for individual budgeted direct service programs reveal wide variances by program, some by over 50%, resulting in the accumulation over a multi-year period of over \$1.4 million in excess net assets.

In its response, TEC indicates that it is inefficient to appropriately track costs by activity. TEC also states that revenues are "highly unpredictable" due to activity changes and unpredictable utilization. However, we noted that TEC tuition policies had appropriate protections for underutilization such as requirements that tuition continue to be paid for the remainder of committed enrollment periods even if an unplanned withdrawal of the student occurred.

In its response, TEC asserts, "TEC actively seeks to minimize income to the collaborative because it is in the best interests of the student and the sending school district." However, this assertion is inconsistent with TEC's statement indicating that its Executive Director should be commended for intentionally increasing TEC's net asset fund balance. In fact, our analysis of individual program prices charged to members and non-members, and our interviews with TEC staff, led us to conclude that TEC did not employ appropriate pricing methodologies based on reasonably projected unit costs and that TEC managers were instead establishing prices in what they described as an "entrepreneurial" manner. As described above, non-member districts were sometimes charged as much as 76% more than member districts, contrary to TEC's bylaws. TEC's generation of such surpluses through the imposition of fees that are significantly in excess of the direct and indirect costs required to provide services clearly seems to conflict with the fee-setting guidance promulgated by DLS and OAG.

In its response, TEC states that it "had been in operation as a 501c 3 organization approved by the IRS and rules for not-for-profits are different than those for Massachusetts municipalities." In fact, although TEC had in the past obtained 501(c)(3) status from the IRS, that status is available to governmental entities as well as to incorporated not-for-profit entities. This status is

granted to governmental entities such as TEC and other education collaboratives that are instrumentalities of governmental units or political subdivisions for the purpose of allowing them to receive tax and other benefits available to other IRS-exempt organizations such as not-for-profit corporations. However, obtaining such IRS status does not in any way exempt a governmental entity from the provisions of state law applicable to governmental entities. Since its creation on May 22, 1974, TEC has always been a Massachusetts education collaborative governmental entity established under the authority of Chapter 40, Section 4E, of the General Laws.

In its response, TEC asserts, “The Executive Director’s comment regarding Millis was misunderstood.” However, we do not agree with this statement. First, the October 3, 2008 minutes of the meeting of TEC’s Board of Directors indicate that the Executive Director had expressed concern regarding the consequences of allowing Millis and two other districts to join the collaborative, apparently due to potential revenue reduction that would occur since the districts would then pay the lower tuition rates established for member districts. The minutes include the following text: “Millis as example: Pays Non-TEC tuition; with three students coming in, almost can’t afford to bring the town in.” Moreover, when we asked the Executive Director about this issue he directly stated that it was not in TEC’s interest to grant the Millis school district membership in the collaborative since TEC was currently making a profit from the higher non-member fees charged to Millis for the services the district purchased from the collaborative.

In its response, TEC states that “Indirect costs in FY08 were allocated on the fairest basis possible, which was equitably based on expected expenditures. Each of the programs incurred approximately 10% in overhead, which was more than a fair charge for each program.” However, the accounting records and budget information provided to us by TEC officials for that fiscal year clearly document that TEC’s indirect costs were not allocated in this manner. Specifically, budgeted indirect costs were allocated on a variable basis across budgeted programs at percentages ranging from as low as 6.0% to as high as 18.8% of budgeted direct program costs. For non-budgeted programs, indirect costs were not allocated, with the exception of an off-budget transportation program provided to one district. In that case, indirect costs were allocated to the program in an amount equal to 72.6% of the program’s total reported direct expense.

During our audit, we asked for documentation of the cost allocation basis used by TEC for its indirect cost allocations. In response, TEC officials provided us only with a document that listed the amount of indirect costs allocated to each program center but did not identify any basis for the allocations. TEC also did not distinctly account for and calculate indirect administrative (management and general) costs and revenues associated with the overall direction and management of TEC's programs. Instead, TEC's indirect administrative expenses and associated revenues were consolidated into a so-called "Core" administrative activity center that also included costs associated with various direct service activities, such as the operation of TEC's cooperative purchasing program. As a result, it was not possible to accurately calculate the total net indirect cost amounts to be allocated across other activity centers. These deficiencies-, involving both the accounting of indirect administrative costs and the absence of an appropriate allocation basis, led us to appropriately conclude that TEC's indirect cost allocation practices were inconsistent and contributed to the organization's overall budgetary control and pricing deficiencies. In our opinion, these budgeting practices and accounting deficiencies effectively undermine the control function ordinarily associated with use of an approved organizational budget and have resulted in TEC member districts and other governmental purchasers of TEC services being charged more than is reasonably necessary to perform services on their behalf during the period covered by our audit.

In its response, TEC makes reference to an email its Treasurer received from an attorney at DLS that states: "unlike city and town departments, collaboratives are not required to turn fund balances over to the general fund at the end of each fiscal year." However, since our audit report had not asserted that any such statutory requirement existed, this information is not relevant to this issue. The email then references the applicability of Chapter 40, Section 4E, of the General Laws to the operation of collaboratives by stating, "The statute also requires that collaboratives operate in accordance with a written agreement entered into by the member townsBeyond this, we cannot advise you whether educational collaboratives are further restricted by the general laws. You may want to explore this further with your legal counsel or the Massachusetts Organization of Education Collaboratives."

We agree with TEC's assertion that it would not be appropriate for the organization to run deficits. However, given that the districts that TEC serves are using their limited funds to pay for TEC's programs and services, it is clearly TEC's responsibility to ensure that its districts pay

a fair but not excessive price for its services. We do not dispute that it is fiscally prudent for an agency's Executive Director to ensure that there are sufficient funds in reserve to cover any unanticipated expenses. However, we do not agree with TEC's assertion that the Executive Director should be commended for increasing TEC's fund balance to the extent that, as of the end of fiscal year 2008, it equaled over 20% of the agency's total annual funding. In our opinion, accumulating the fund balance to this level, which TEC admits was "unusually high," was excessive and therefore not in the best interest of TEC's member districts or consistent with DLS and OAG guidance. In this regard, in its response, TEC asserts "There is nothing that has been written into Massachusetts General laws that indicates that collaboratives are subject to DLS and OAG in the same fashion as a municipality." We acknowledge that nothing came to our attention in state law that either specifically includes or exempts education collaboratives such as TEC from DLS and OAG regulations and other requirements such as how fees should be established. However, subsequent to the end of our audit fieldwork, we spoke with the Chief of the Bureau of Municipal Finance Law within DLS regarding this matter. During our conversation, the Chief stated that although DLS does not have statutory authority to itself write regulations governing collaboratives, she would question any assertion that collaboratives are exempt from municipal finance law or other laws that would be applicable to collaborative activities if they were instead directly conducted by school committees. The only exception would be education law applicability exceptions directly written into Chapter 40, Section 4E, of the General Laws. The Chief continued to state that if any collaborative were to formally raise the question of exceptions to municipal finance law or to litigate the issue, the obvious legal position likely to be taken by the Commonwealth would be that, since collaboratives are created by and governed by school committees, they are subject to the same requirements applicable to school committees except where statutory provisions or other evidence demonstrates legislative intent to exempt collaboratives from otherwise applicable requirements. The Chief told us that, absent authorization to the contrary, governmental entities are precluded from doing together what they cannot do alone and that DLS sees no reason to think that legislative intent was to permit a situation whereby school committees can use collaboratives to legally do through the collaboratives what they cannot legally do on their own. Finally, the Chief stated that her understanding is that the OAG has not gotten involved in any of these issues or provided any special guidance or exceptions to guidance provisions for collaboratives.

Based on this information, we believe that TEC's assertions questioning the applicability to education collaboratives of municipal finance laws and DLS and OAG guidance are without merit, and we again recommend that TEC immediately take action to implement our audit recommendations unless formal guidance is received from DLS, DESE, or the OAG that corrective action is not required. If TEC believes that it is necessary for it to maintain a fund balance derived from sources other than donations or other non-fee revenue to ensure its solvency and its ability to access credit, it should determine in consultation with DLS, DESE, and TEC's member town governments what amounts might be reasonable and permissible under municipal finance law, and what controls should be established to ensure that excessive fees are not charged and that any significant excesses of revenue over expense are returned to purchasers either directly or through fee reductions during the following fiscal year.

3. INADEQUATE CONTROLS OVER FOOD AND MEETING EXPENSES RESULTED IN AS MUCH AS \$59,267 IN UNNECESSARY AND UNALLOWABLE EXPENSES

DOR, through DLS, has established guidance for all municipal governmental organizations, including education collaboratives that recommends that these entities establish clear guidelines or policies relative to their allowable expenses. However, we found that during the period covered by our audit, TEC had not established such guidelines or policies. As a result, we determined that TEC incurred as much as \$59,267 in expenses for food and entertainment at Superintendent retreats and various other meetings and holiday parties that appeared to have been unnecessary and not consistent with DLS guidance on allowable governmental expenses. Included in this amount is as much as \$1,809 for the purchase of alcohol at two Superintendent retreats, which are specifically prohibited by state law.

Neither Section 4E of Chapter 40 of the General Laws, which provides for the establishment of education collaboratives, nor DESE regulations establish guidelines on allowable expenses that can be incurred by education collaboratives. However, DLS has provided guidance to local government entities and has recommended that each entity establish specific internal policies or guidelines on allowable expenses. For example, DLS's newsletter, City and Town, Volume 19, No. 2, published in February 2006, states in part:

DLS strongly recommends that municipalities develop clear written policies or guidelines, preferably by bylaw or ordinance, about allowable expenditures. . . . Travel expenses are often set out in collective bargaining agreements, but the municipality should also adopt a policy to cover travel expenses for non-union employees. DLS also recommends that

standards be established for merit awards, food or fundraising expenses. DLS also recommends that accounting officers advise managers and employees at the beginning of each fiscal year of the municipality's policies. This will help to avoid uncertainty or disagreements about whether certain expenditures are permissible and payable.

DLS's guidance also states that expenditures by municipal entities can only be made for proper public purposes, providing no more than incidental minor benefits to individuals in limited situations where the expenditure of public funds advances both public and private interests. This guidance requires municipalities to employ generally conservative practices relative to the types of expenses they deem allowable. For example, according to this guidance, funding of modest lunches should be permitted only in conjunction with all-day meetings. In addition to the DLS guidance previously noted, TEC's current collaborative agreement originally approved by TEC member districts and DESE in 1980 requires that:

No funds received by TEC on account of this Agreement may be expended for any purpose or use not provided for by said budget unless such expenditure shall first have been approved by the Board.

As a result, any expenditure made by TEC that was not specifically budgeted or formally approved by TEC's board would be considered unallowable in accordance with the terms and conditions of the collaborative agreement.

During our audit, we reviewed the internal controls TEC had established relative to expenditures for food and meeting expenses. Based on our review, we determined that, contrary to DLS guidance, TEC had not established any formal controls (e.g., written policies and procedures), relative to its food and meeting expenses. Consequently, we analyzed the documentation TEC was maintaining relative to the \$81,859 in expenses it incurred for food and meeting during the period July 1, 2006 through November 25, 2008. Based on our review of this information, we identified the following issues with \$59,267 of these expenses:

a. Unnecessary and Unallowable Superintendent Retreat Expenditures Totaling as Much as \$28,135

According to TEC's records, TEC sponsors an annual event which it refers to as a "superintendents' retreat" in mid-May of each year. During the two years covered by our audit, these retreats were held at the Ocean Edge Resort and Club in Brewster, Massachusetts. TEC paid \$9,673 for the 2007 retreat and \$15,462 for the 2008 retreat, and in August 2008 made a \$3,000 deposit to the same resort for a retreat scheduled to be held May

13 through May 15, 2009, bringing the combined total retreat expense during our audit period to \$28,135. A summary of the expenses incurred by TEC for its fiscal year 2008 retreat appears below:

**Expenditures and Reimbursements for Superintendents' Retreat
May 2008**

Direct payments to resort	\$11,179
Speaker fees to two Boston University professors @ \$750 each	1,500
Wildlife sanctuary boat tour	600
Van rental related to boat tour	450
Reimbursement to Executive Director for retiree gifts	470
Reimbursement to Executive Director for alcoholic beverages and related charges (e.g., bar setup fees)	<u>1,263</u>
Total known retreat expense excluding employee time and associated overhead costs	\$15,462
Total retreat expenses reimbursed by member districts	<u>7,415</u>
Expenses absorbed by TEC	<u>\$8,047</u>

Based on our review of the expenses associated with these two retreats, we identified the following issues:

- Although there was a minor training component to these retreats, the majority of the expenses incurred appear to be for food, lodging, and entertainment. For example, during the May 2008 retreat, there were two guest speakers who gave lectures, each scheduled to last only three hours. There was no other documentation that any TEC business was conducted. In our opinion, since TEC member districts are all adjoining suburbs, it would have been more cost effective to have held these retreats at TEC's offices or at a nearby school district facility or similar venue such as a community college. Further, other expenses associated with these retreats such as those associated with golf and tours, are not consistent with DLS's guidance regarding public purpose, necessity, and reasonableness. Also, the associated costs and offsetting revenues for these retreats were not included with reasonable detail as a separate item in TEC's annual budgets or submitted to the TEC Board of Directors for special approval as required by the TEC collaborative agreement.
- Chapter 44, Section 58, of the General Laws prohibits the use of public funds to purchase alcohol and tobacco by stating "No city or town shall pay a bill incurred by any official thereof for wines, liquors or cigars." However, our review found documentation indicating that, for these two retreats, TEC had reimbursed its Executive Director \$1,809 in expenses for alcohol-related purchases incurred on behalf of town school superintendents and himself, which had been ambiguously labeled (e.g., as "group services") in his reimbursement claims.

- TEC did not charge all participants the same amount for the retreats. For example, for the 2008 retreat, some districts' participants were charged as much as \$860 per person; five participants, including two TEC managers and three retired or incoming TEC member district superintendents, were not charged; and another superintendent's district was charged a reduced rate of \$110. The \$110 invoice to the district for this superintendent covered only partial expenses associated with his golf, even though the individual had also attended the retreat for two nights. In addition to not charging all participants in an equitable manner, the process of directing all retreat related charges through TEC effectively bypassed any town or school district policies and reporting/approval requirements that may have been established as called for by the above-quoted DLS guidelines regarding allowable expenditures. Taxable benefits or gratuities received by participants may also not have been reported to state and federal authorities as would be expected to occur if the benefits had been directly paid to participants by individual school districts rather than through the collaborative.

Regarding these matters, TEC's Executive Director stated that the costs associated with the retreats were, in his opinion, for professional development and therefore appropriate. The Executive Director also stated that he and his staff were unaware of the DLS guidance and the prohibition on alcoholic beverage expenditures and that, if he had known that the alcoholic beverage expenditures were prohibited, he would not have charged them to TEC.

b. Potentially Excessive Meeting and Food Expenditures Totaling as Much as \$31,132

As previously noted, DLS guidance advises municipal organizations to utilize conservative practices for establishing allowable expenses. Examples of such conservative practices include the use of private rather than public funds for retirement parties, and the provision of only minimal refreshments at meetings as needed to keep meeting participants alert and to avoid loss of time and disruption if participants leave the premises. According to DLS guidelines, funding of meals such as modest lunches is appropriate in conjunction with all-day meetings, but not short duration meetings. During our review of the documentation TEC was maintaining relative to its food and entertainment expenses, we noted that during our audit period, TEC incurred meal expenses that primarily fell into two categories. First, we found that TEC often purchased food for school programs such as for culinary arts classes, and also provided reimbursements to staff for food for programs directly serving students. In our opinion, these types of food expenses, which totaled \$10,962 during our audit period, were reasonable and consistent with DLS guidance. Second, we noted that TEC incurred various expenses for food and related costs for employees and individuals other than students. We analyzed those expenditures to assess their consistency with DLS

guidance. Specifically, we looked for documentation to substantiate that these expenses were reasonable and necessary for a public purpose and that food and related items were for all-day meetings, public events such as open houses, or other appropriate purposes such as reimbursing employees for reasonable meal costs during travel and attendance at out-of-town conferences.

Based on our review, we did not question \$19,078 of these expenses since they appeared to be reasonable and for appropriate purposes. However, the majority of these non-student-related expenditures, which totaled \$31,132 for costs other than the above described Superintendent's Retreats, were for items that appeared to be inconsistent with DLS guidance in that they were purchased for short-duration meetings of employees of TEC or school district representatives. These expenditures also included food for TEC Board of Directors meetings, short duration superintendent meetings held at the Wellesley College Club, various other short duration meetings, two holiday parties totaling \$3,343, and reimbursements to the Executive Director such as those for lunch or dinner restaurant meals. The reimbursements to the Executive Director lacked sufficient documentation to establish that the expenditures were necessary for carrying out the public purposes of the collaborative. The table below summarizes the questionable expenses we identified during our review in this area:

Questionable Food and Meeting Expenditures*

July 1, 2006 through November 25, 2008

	Fiscal Year 2007	Fiscal Year 2008	Fiscal Year 2009 through 11/25/2008	Total
Holiday parties	\$2,148	\$1,195	0	\$3,343
Short duration meetings, Executive Director meals, etc.	<u>9,425</u>	<u>14,418</u>	<u>\$3,946</u>	<u>27,789</u>
Total questioned expenditures	<u>\$11,573</u>	<u>\$15,613</u>	<u>\$3,946</u>	<u>\$31,132</u>

* Excludes expenditure amounts already included in the audit results regarding Superintendents' Retreats.

Recommendation

TEC should take measures to ensure that government funds are used only for purposes consistent with DLS guidance and should seek recovery of unallowable expenditures such as the alcoholic beverage reimbursements and excessive gratuities related to the Superintendents' Retreats. Further, TEC should develop and implement adequate internal controls over its expenditures for meals and entertainment that are consistent with DLS guidance.

Auditee's Response

In response to this issue, TEC officials stated, in part:

The job-alike meeting expenses were formally adopted as a part of TEC annual budgets. However, if it is found that these expenses are inappropriate, TEC will cease spending on these nominal lunches and superintendent retreats. The holiday parties were intended as an appreciation for all staff and were not excessive. The total amount would average out to less than \$13 per employee for an annual event to create goodwill. The past purchase of alcohol at the "Superintendents' Conference on Technology and Team Building" was repaid by the participating superintendents from their own personal funds and past practices have been ended in accordance with state law.

Auditor's Reply

As noted in our report, we found that during the period covered by our audit, TEC incurred as much as \$59,267 in expenses for food and entertainment at Superintendents' retreats and various other meetings and holiday parties that appeared to have been unnecessary and not consistent with DLS guidance on allowable governmental expenses. Included in this amount is as much as \$1,809 for the purchase of alcohol at two Superintendent retreats, which is specifically prohibited by state law. In its response, TEC characterized the expenditures on lunches and superintendent retreats as "nominal." However, these expenditures occurred on a routine, recurring basis, resulting in the cumulative expenditure of significant public funds for purposes that are contrary to DLS guidelines. Although some of these expenses, such as food expenses for meetings, may have been budgeted by TEC staff, given the fiscal problems many of TEC's school district are facing, TEC clearly needs to take measures to identify and eliminate any unnecessary expenses, particularly those which are not consistent with DLS guidance.

Finally, in regard to the holiday parties, we do not question that such parties help foster goodwill amongst staff. However, in our opinion, since the cost of such parties is minimal on a per-participant basis, it should more appropriately be borne by TEC's employees and not the taxpayers from TEC's member districts.

4. UNLICENSED OR INADEQUATELY QUALIFIED TEACHERS AND SERVICE AND SUPPORT STAFF

According to Chapter 40, Section 4E, of the General Laws, certain categories of education collaborative employees, such as teachers, guidance counselors, and school psychologists, are required to be licensed by DESE. Other statutes provide for licensure by the Commonwealth's Division of Professional Licensure (DPL) for certain clinical professionals such as occupational therapists. Despite these requirements, we found that during our audit period a number of TEC's staff did not meet these mandated licensing requirements. In some cases, TEC employees were simply not licensed, whereas in other cases they were not properly licensed for the particular areas in which they were teaching. Specifically, during our review of the personnel records of 52 past or present TEC educators subject to DESE licensure requirements, we identified licensing issues for 29 of these 52 educators. In addition, we were unable to verify through TEC's records that two other employees -- a speech therapist and an occupational therapist -- had been properly licensed by DPL. Finally, the special legal status of education collaboratives such as TEC has resulted in exceptions to licensing requirements for certain staff who would otherwise be required to have DESE licenses if they were working in regular public schools.

Although education collaborative teachers must be licensed by DESE, their supervisors working in positions comparable to principals, department heads, special education administrators, and superintendents, are generally exempt from DESE licensure requirements that would otherwise apply if they were working directly in a public school system. Collaborative Boards of Directors have the authority to establish qualification standards for these exempt employees, as well as supplemental standards for employees who are subject to DESE's licensure requirements. Nevertheless, we found that TEC and its board have not established a formal system of personnel policies, including job classifications and qualification requirements for all its positions, including those not subject to DESE licensure. As a result, certain members of TEC's administrative staff may not be held to the same job qualification standards that apply to staff working in public school districts and charter schools within the Commonwealth in that hold similar positions. The specific issues we identified in this area, are discussed below:

a. Unlicensed or Inadequately Licensed Staff

Educators and administrators working directly for Massachusetts public school districts, are subject to comprehensive certification requirements established by Chapter 71 of the General Laws. Pursuant to this statute, DESE has promulgated regulations and approval systems using the term “licenses” in its regulations. This licensure system is designed to cover certain positions, including teachers working in specific subject areas, grade levels, or with specific student populations (e.g., students with severe disabilities); support positions (e.g., guidance counselors, school psychologists, school nurses), and administrative positions such as supervisors/directors, principals, special education administrators, school business administrators, and superintendents. These regulations also provide for a waiver process administered by DESE to approve exceptions to licensure requirements on the basis of individual circumstances such as a district’s inability to recruit properly licensed teachers for specialized activities. These licensure requirements have also been applied, by statute and regulation, to other public education settings such as regional school districts and charter schools. However, DESE officials stated that TEC and other education collaboratives are exempt from certain licensure requirements, since Chapter 40, Section 4E, of the General Laws, which establishes education collaboratives as independent local governmental entities, does not expressly mandate adherence to all regular public school licensure requirements. Specifically, Chapter 40, Section 4E identifies only certain educator positions as subject to licensure and is silent regarding the applicability of licensure requirements to positions not listed in the statute, as follows:

No person shall be eligible for employment by said board of directors as an instructor of children with severe special needs, teacher of children with special needs, teacher, guidance counselor or school psychologist unless such person has been granted a certificate by the board of education under the provisions of section thirty eight G of chapter seventy one or section six of chapter seventy one A or an approval under the regulations promulgated by the board of education under chapter seventy one B or chapter seventy four with respect to the type of position for which he seeks employment; provided, however, that nothing herein shall be construed to prevent a board of directors of an education collaborative from prescribing additional qualifications. A board of directors of an education collaborative may, upon its request, be exempted by the board of education for any one school year from the requirements of this section to employ certified or approved personnel when compliance therewith would in the opinion of the board constitute a great hardship.

DESE officials stated that they interpret this statutory language to effectively exempt from licensure collaborative positions other than those expressly identified by the statute, except

for certain positions in specially licensed alternative schools. Even business administrators and Executive Directors at education collaboratives are not required to be licensed by DESE unless the individual collaborative's Board of Directors has voluntarily prescribed DESE licensure as a qualification requirement for the position. This situation can result in situations whereby teachers are required to be licensed while no qualification requirements exist for their supervisors. Due to the special employee licensure and qualification situation applicable to education collaboratives, we designed our audit testing in this area to TEC employees subject to DESE and/or DPL licensure (e.g., speech and occupational therapists).

During our audit, we reviewed staff directories and personnel records covering TEC's employee base of approximately 132 full- and part-time employees per year. We used this information to select a sample of 80 personnel files of individuals employed at TEC during fiscal years 2007 through 2009. Within this sample were 11 past and 41 present TEC employees who we determined were subject to DESE licensure requirements by virtue of their position titles or other personnel record information. During our review of these individuals' personnel records, we found that there was either inadequate documentation of licensure or actual evidence of licensing issues (e.g., no requests for license waivers) for as many as 31 of these staff members. In order to verify the licensing status of these individuals, we then took a subset of 22 of these 31 files and had a member of TEC's staff verify their licensure status using DESE's licensure database. This further analysis determined that at least 20 of the 22 (90.9%) had licensing issues. For one other teacher, documentation regarding the individual's education role was not sufficient for us to determine whether all DESE licensure requirements had been met. The licensing issues we identified included TEC's hiring of teachers without current valid licenses in place for at least part of the time the teacher was employed at TEC and its using teachers licensed only in one activity area to teach in a different area requiring a different type of license. This is a concern since DESE licenses teachers for specific activity areas, and, with limited exceptions, teachers must be properly licensed in each area.³ For example, a teacher licensed to teach only at the elementary grade levels might be employed by TEC as a middle school teacher, or a teacher might need to be licensed for both English and for teaching students with moderate disabilities, but might only be licensed for teaching English.

³ The principal exception allows teachers to spend up to 20% of their time working outside the scope of their licensed area. Our audit factored in such permissible activities.

We also noted that, in many instances, TEC would obtain a DESE waiver for a particular staff person but then would not adhere to the waiver conditions. For example, one characteristic of the DESE waiver system is that, although waivers are routinely granted for an initial year of a staff person's employment, DESE generally requires that in order to receive a waiver for an employee to remain in the position on a multi-year basis, the employee must demonstrate progress in completing licensure requirements such as fulfilling teacher coursework requirements and passing applicable components of licensure qualification tests. However, instead of complying with these waiver requirements, TEC sometimes employed individuals on a multi-year basis without submitting a waiver request. For example, TEC employed one Mathematics teacher in a setting requiring licensure in both Mathematics and Moderate Disabilities. The teacher was hired in September 2004 and was still working in this position during the time we were conducting our audit fieldwork in 2009. DESE records showed that the teacher had applied for licensure in both Mathematics and Moderate Disabilities in October 2007 but that DESE had determined that he was "not ready" for licensure and his application remained in that status as of the end of our audit fieldwork in 2009. There was no documentation that TEC had sought a waiver to use the individual as a teacher until September 22, 2008 when a waiver for Initial Mathematics was obtained by TEC to employ the teacher through June 30, 2009. However, there was no indication in TEC's records that it had been disclosed to DESE that the employee was not a new hire and had already been teaching at TEC for multiple years without either a valid license or a waiver. Moreover, there was no indication that DESE had been asked to waive the applicable Moderate Disabilities licensure requirements of the position in which this individual was teaching.

DESE licensing unit staff explained to us that initial single-year waiver requests are routinely granted on the assumption that requesting employers are following all applicable waiver rules. When requests are made to renew waivers for subsequent years, DESE imposes additional requirements for demonstration of satisfactory progress toward licensure and frequently conducts desk reviews of such waivers. Had TEC sought waivers for the teacher in question at the time of hiring and for each year thereafter, TEC would have been required to replace the teacher unless progress toward completion of licensure requirements had been demonstrated to DESE's satisfaction. Even when waivers were obtained, TEC generally had no documentation showing that it had complied with waiver conditions such as the rule

requiring that positions be advertised in an effort to obtain alternative candidates not requiring waiver approval and that documentation be retained on why the collaborative did not hire candidates meeting licensure requirements. In discussing this situation with TEC managers, one school director acknowledged that, in cases where it was believed that an existing unlicensed or inadequately licensed teacher worked well with students, TEC disregarded licensure requirements and waiver approval conditions.

The following table summarizes our results regarding licensure waiver issues for the 29 individuals remaining in our sample subset of 31 educators with apparent licensing issues after adjusting for the two individuals we found to be properly licensed despite the failure of TEC to retain appropriate documentation:

Summary of Waiver Issues*

Waiver Issues	Number of Employees
Waiver request not made for an unlicensed teacher	14
Waiver requests not made for an improperly licensed teacher even after one or more years of employment	9
Waivers obtained but waiver conditions were not met, or only partial waivers were obtained	<u>6</u>
Total	<u>29</u>

* Note most of the 20 individuals we identified as having no license or an inappropriate license are also included in the table above as also having license waiver issues.

In addition to the above DESE licensure issues, we identified potential compliance issues involving employees required to be licensed through the Commonwealth's Division of Professional Licensure (DPL). Specifically, during the period of our review, 13 individuals were employed by TEC in positions requiring DPL licensure, such as speech and language pathologists, physical therapists, or occupational therapists.⁴ TEC records and tracking systems lacked adequate documentation that these 13 individuals held currently valid DPL licenses. We therefore reviewed DPL licensure status information available to the public on

⁴ These Speech Language Pathologist licensure requirements overlap with DESE Speech, Language, and Hearing Disorder Specialist educator licensure requirements. DESE indicated that individuals working in these positions are required to hold both DESE and DPL licenses. This differs from licensure arrangements for school physical therapists and occupational therapists, who are required only to hold DPL licenses. As a result, there is a partial overlap between this set of employees and the sample of 52 employees subject to DESE licensure requirements.

the Internet and were not able to match the employee names for two of the employees to names in the DPL licensure database, which may indicate that these two individuals were not properly licensed.

b. TEC Has Not Established Standard Qualifications for Its Non-licensed Staff

As described above, many employees, such as supervisors and senior managers at TEC and other education collaboratives who would be subject to DESE licensure requirements if they were working in regular public schools or charter schools, are treated as exempt from licensure due to the special legal status of education collaboratives. However, as previously detailed, Boards of Directors of collaboratives have the authority to establish qualification standards for these exempt employees, as well as any supplemental standards for employees still subject to licensure requirements. Despite this statutory authority, we found that TEC has not established a formal system of personnel policies including job classifications and qualification requirements for all its positions. During our audit, we reviewed a sample of the personnel files of TEC employees working in positions not subject to DESE licensure during fiscal year 2009. During our review, we identified at least seven individuals in positions where their counterparts in regular school settings would be subject to DESE licensure requirements. These positions include TEC's Executive Director, Assistant Executive Director/Administrator of Student Services, the incoming Administrator of Student Services⁵, the Administrator of Finance and Operations, and three Network Directors responsible for directly supervising classroom teachers and related specialists and aides. We noted that, although not required, four of these seven individuals did hold DESE licenses appropriate for the functional roles of their positions. However, although TEC's Executive Director had, worked in the past as a superintendent in other states, he did not have a Massachusetts DESE license and two other administrative staff members (the Assistant Executive Director and one Network Director) did not have a DESE license for the position in which they were working.

We also found that TEC had not established qualification requirements for members of its staff who provided Applied Behavior Analysis (ABA) services. TEC and many other

⁵ A new Administrator of Student Services was hired in anticipation of the July 2009 assumption of the Executive Director's role by the existing Assistant Executive Director/Administrator of Student Services. However, we verified that the individual appears to be appropriately qualified with current DESE licensure as both a Special Education Administrator and as a Superintendent/Assistant Superintendent.

educational organizations in the Commonwealth provide ABA-type behavior intervention services to their students, including those with autism spectrum disorders. TEC has established a distinct program to provide these services both in the classroom and other TEC program settings and through out-of-school home-based services to students and their families. The program operates with a coordinator/supervisor, five additional supervisors, and other staff classified as “behavior therapists.” With the exception of senior program staff, most of the staff provide behavior therapy services on a part-time basis. Although the TEC staff directory only identifies a total of 11 individuals as primarily working for the program, a total of 30 individuals were paid for providing at least some program services during the first five months of fiscal year 2009.

DESE acknowledged that the issue of defining appropriate qualification requirements for individuals carrying out these activities is an issue across the Massachusetts public education system, not just for education collaboratives, and that DESE has not yet determined the most appropriate approach to establishing licensure or alternative qualification standards. As a result, we believe that it is particularly important that TEC establish appropriate qualification standards for individuals providing these services.

Recommendation

TEC should take measures to ensure that it fully complies with DESE and other Commonwealth staff licensure requirements and should establish a formal system of internal qualification requirements for professional and direct service positions (e.g., educational administrators and ABA program staff) that are not subject to mandatory state licensure requirements. Further, in cases where TEC uses staff subject to DESE waiver provisions, all waiver conditions should be adhered to and adequately documented.

Auditee's Response

All teachers employed by TEC are in fact fully licensed or have a current approved waiver from the DESE. These documents may not have been in individual employee folders as the personnel department had some changes in staffing at the time of the audit and documents on individual staff members were being reviewed and worked on. All files have been updated. TEC has developed a computerized system to track the renewal of licenses and certifications and all documentation of employees is on file in the office of the HR Coordinator.

Auditor's Reply

Contrary to what TEC implies in its response, our report did not conclude that the licensing status of various educational professionals at TEC was deficient because some documents happened to be missing from personnel files. Rather, as noted in our report, we not only reviewed the licensing information in these individuals' personnel files but also, with the assistance of TEC's staff, confirmed the licensing status of the individuals in question using online DESE licensure records. As noted in our report, our audit work in this area identified that numerous TEC employees subject to DESE licensure requirements were not fully or properly licensed or in approved waiver status. Further, during our audit, a number of TEC's staff mentioned that they were aware of certain staff not being properly licensed. Finally, we note that TEC's response does not address our concern that TEC has not established standard qualifications for its non-licensed staff. As such, we again recommend that TEC implement our recommendations relative to this issue.

5. NONCOMPLIANCE WITH STATE REGULATIONS RELATIVE TO THE EVALUATION OF TEACHERS AND ADMINISTRATORS

DESE regulations require education collaboratives such as TEC to develop appropriate employee performance standards and to conduct staff evaluations, which are to be documented in writing. According to these regulations, administrators and teachers without professional teacher status are to be evaluated at least annually, whereas those with professional status are to be evaluated at least once every two years. The stated purpose of these regulatory requirements is to assure effective teaching and administrative leadership in the Commonwealth's public schools. However, we found that TEC had not established appropriate performance standards for its employees and that there was no documentation substantiating that TEC was conducting the required performance evaluations of its staff, including its Executive Director. Without such documentation, there is inadequate assurance that TEC is meeting its responsibility to the Commonwealth.

In 1995, DESE promulgated revisions to 603 Code of Massachusetts Regulations (CMR) 35.00 entitled "Evaluation of Teachers and Administrators" and issued 13 pages of accompanying guidance relative to staff performance standards. These materials provide school committees, administrators, and their counterparts at education collaboratives with detailed requirements for the development of formal performance standards and comprehensive performance evaluation

systems. These regulations require that administrators and teachers without professional teacher status be evaluated at least annually, whereas those with professional status be evaluated at least once every two years. All activity, including specific measurable performance standards allowing for significant differences in assignments and responsibilities, the purpose of the evaluation, evaluation results, and employee responses to the evaluation, are required to be documented in writing.

The importance of these regulatory requirements is stressed in accompanying DESE guidance, which states in part:

The purpose of 603 CMR 35.00 is to ensure that every school committee⁶ has a system to enhance the professionalism and accountability of teachers and administrators, which will enable them to assist all students to perform at high levels. 603 CMR 35.00, together with the Principles of Effective Teaching and Principles of Effective Administrative Leadership adopted by the Board of Education, set out what Massachusetts teachers and administrators are expected to know and be able to do. 603 CMR 35.00 requires that school committees establish a rigorous and comprehensive evaluation process for teachers and administrators, consistent with these principles, to assure effective teaching and administrative leadership in the Commonwealth's public schools.

The 1993 Education Reform Act also provides for the use of so-called “induction” or mentoring activities for new educators as a means of augmenting professionalism and accountability systems to improve the quality of education in the Commonwealth. These induction activities are closely related to licensure systems, since DESE educational licensure regulations (603 CMR 7.00) require completion of the induction process in order to obtain professional teacher licensure status. However, the induction process is also closely related to supervision and performance evaluation systems, since induction activities include classroom observation and meetings with a support team whose composition must include a trained mentor and administrator qualified to evaluate teachers.

In 2001, DESE published 24 pages of specific guidelines for the operation of induction activities. Those guidelines expressly incorporate the performance evaluation of beginning teachers into the induction process and mandate that beginning teachers be given a copy of applicable performance standards, an explanation of the evaluation instrument, and information on when and how often evaluations will occur. However, despite these requirements, during our

⁶ For the purpose of the regulation, the term “school committee” is defined to include not just school committees for regular school districts but also the governing bodies of regional and agricultural school districts, education collaboratives, and charter schools.

audit of TEC we found no evidence that the required performance standards and evaluation and induction systems exist at TEC. When we reviewed TEC's policies and procedures and personnel records, we found no evidence that TEC had established the required performance standards for all educators and administrators or had documented the completion of evaluations or other supervisory or induction/mentoring activity.

Despite this failure to adhere to DESE requirements, we noted that the personnel file for one employee included a certification document sent to DESE by the TEC Administrator of Student Services attesting to the completion of induction and teaching experience requirements for the employee's application for licensure at the professional status level. Not only was there no documentation in the personnel file of underlying induction program activity; but TEC records also showed that the teacher had been employed teaching out of a licensed area without a waiver, and the teaching area had been misstated in the certification document. Also, there was no documentation to substantiate that TEC's board had formally evaluated the performance of the Executive Director. When we interviewed employees, including the Executive Director, Assistant Executive Director/Administrator of Student Services, and the Administrator of Finance and Operations regarding this matter, these individuals stated that no such documentation existed other than for one employee whose supervisor had documented significant problems with this employee's performance. These officials stated that this was because all performance evaluation and supervisory/induction activity was conducted at TEC on an informal verbal basis without documentation. These officials also stated that this was because TEC is a small operation and that more formal documented systems were, in their opinion, not needed. However, DESE regulations and guidelines do not provide for any exceptions to the aforementioned staff evaluation and induction documentation requirements. Without such documentation, there is inadequate evidence to substantiate that TEC is complying with DESE regulation in this area.

Recommendation

TEC should take the measures necessary to ensure that it is fully complying with the requirements of 603 CMR 35.00 relative to staff evaluation and with DESE induction guidelines.

Auditee's Response

TEC did not provide any written comments relative to this matter.

6. TEC'S BOARD WAS NOT ADEQUATELY INFORMED OF AS MUCH AS \$125,832 IN CONSULTING EXPENDITURES, INCLUDING AS MUCH AS \$108,000 IN LEGISLATIVE AGENT SERVICES

According to its collaborative agreement, all TEC expenditures are required to be included in its annual budgets approved by its board, or where that has not been done, must be expressly approved by the Board of Directors. However, we found that between July 1, 2006 and November 25, 2008, TEC managers expended at least \$113,832 (\$96,000 for legislative agent services, and \$17,832 for legislative tracking and other outside consulting services) that had been excluded from board-approved budgets. All of these expenses were accounted for in TEC's accounting system in a non-budgeted account entitled "Government Consult." In addition, public disclosure filings made by TEC's legislative agent to the Public Records Division of the Commonwealth's Office of the Secretary of State indicated that an additional \$12,000 was expended for legislative agent services through December 31, 2008. TEC's Executive Director claimed that although all these expenditures were unbudgeted he had obtained board approval for them. However, our review of the minutes of the meetings of TEC's board indicated that TEC's Executive Director advised the board that he was procuring legislative agent services only after he had contracted for them and that there was no indication in these minutes that the board had formally approved any expenditure amounts for these services. In fact, according to its Chairperson, the TEC board was unaware that payments totaling \$96,000 for legislative agent services had been recorded in the general ledger through November 25, 2008 and she stated that it was her recollection that the board had been led to believe that these expenditures would total only approximately \$20,000. Although payments for these types of services are allowable under normal circumstances, the failure by TEC's administrative staff to include these expenditures in board-approved budgets or to properly document alternative board approval of these expenditures is a violation of the TEC collaborative agreement.

As described in Audit Results No. 2 regarding budgetary control deficiencies, we determined that, despite the requirements created by the TEC collaborative agreement, TEC has not established a comprehensive annual budget covering all collaborative operations. Significant gaps have included, but have not been limited to, grant operations and expenditures for the services of legislative agents, commonly known as lobbyists. Since October 25, 2006 TEC has expended significant collaborative resources on payments for a legislative agent and for additional legislative tracking services and consultant services on behalf of TEC and its

members. Although the Executive Director sought and obtained an August 9, 2006 review by TEC's legal counsel affirming the general legality of paying for legislative agent services under applicable state law,⁷ the failure to include expenditures for these services in board-approved budgets or to properly document alternative informed board approval of the expenditure amounts was a violation of the TEC collaborative agreement.

Our review of fiscal year 2007 budget documentation and minutes for the June 2, 2006 Board of Directors meeting, at which the TEC collaborative agreement was updated and ratified for the coming fiscal year, found no reference to plans to contract for these services during the fiscal year beginning July 1, 2006 or documentation of board authorization for associated expenditure amounts. In fact, minutes for the first meeting of the fiscal year, held on October 13, 2006, show that the Executive Director simply announced:

TEC has contracted with a lobbyist in an effort to move forward with [the Executive Director's] list of legislative priorities: 1) Statewide Cooperative Purchasing; 2) SPED [Special Education] Transportation Costs; 3) State Funding of Facilities; and 4) Reform of Ch 70 [MGL c. 70, School Funds and State Aid to Public Schools].

No dollar amount or duration for the contract was specified, and no vote was taken to approve the expenditures. Instead, the minutes state:

The School Committee representatives continued to meet with [the Executive Director] and TEC's lobbyist . . . in their job-alike meeting.

The only reference to funding arrangements for the legislative agent services appears in a January 11, 2008 report regarding review of the proposed budget for fiscal year 2009, which simply states that the Executive Director "reported that the costs related to legislative services that TEC utilizes come from the fund balance."

In addition to the legislative agent expenditures described above, the General Ledger showed \$17,832 in payments to three other businesses between July 1, 2006 and the November 25, 2008 cut-off date for general ledger entries examined by our audit. Of this amount, \$7,000 was for an Internet-based legislative tracking service, \$500 was for the services of a public relations firm,

⁷ Under state law, only certain legislative agent/lobbying activities, such as advocacy on behalf of ballot initiatives, are prohibited. The activities documented by the board minutes did not appear to fall under any state prohibitions. In contrast, federal grant conditions prohibit the use of federal funds for the activities conducted on TEC's behalf. However our review of TEC's accounting records found no evidence that federal grant funds received by TEC were used to support TEC's legislative agent activities.

and \$10,332 was for the services of an educational consulting firm. These expenditures are summarized in the table below:

**Non-Budgeted "Government Consult" Expenditures
July 1, 2006 through November 25, 2008**

Firm	Services	Fiscal Year			Total
		2007	2008	2009 through November 25, 2008	
Capitol Strategies, LLC *	Legislative Agent	\$36,000	\$44,000	\$16,000	\$96,000**
Capitol Advantage, Inc.	Legislation Tracking	3,250	3,750	0	7,000
Strategy Group, Inc.	Public Relations	500	0	0	500
Comprehensive Educational Services, Inc.	Educational Consulting	<u>0</u>	<u>10,332</u>	<u>0</u>	<u>10,332</u>
	Total	<u>\$39,750</u>	<u>\$58,082</u>	<u>\$16,000</u>	<u>\$113,832</u>

* While payments were made to this firm, the firm identified in the board minutes was a different firm operated by one of the three principals of Capitol Strategies, LLC.

** As described in the accompanying report text, Secretary of State lobbyist filings indicate that the amount paid through December 31, 2008 totaled \$108,000, which is \$12,000 more than the amount paid through November 25, 2008 and recorded in the general ledger as of that date.

As previously discussed, since TEC's board minutes did not indicate that these expenditures had been appropriately budgeted and approved by the board each year, we interviewed TEC's board Chairperson, who expressed surprise that \$96,000 was paid to the legislative agent. When we related that communication to the Executive Director, he also provided no explanation for the off-budget nature of the expenditures but insisted that the board had in fact approved the expenditure of \$4,000 per month for lobbying services throughout the entire multi-year period.

Regarding this matter, TEC's Executive Director defended the off-budget legislative agent expenditures by asserting that they were low and he asked a TEC member district superintendent to provide us with additional input. The superintendent told us that, in his opinion, members of TEC get the lobbying investment back "10 times over" and that the activity helps "ensure that suburban communities get their fair share up on the hill." The superintendent also added that although he did not remember the actual extent to which the lobbying activity had been processed with the board, he did not think it should come as a surprise to anyone since the TEC superintendents have had extensive discussions on the lobbying activity during their regular monthly meetings.

Recommendation

We recommend that the expenditures in question be recovered if possible and returned to TEC member districts, and that TEC obtain and document all budget and board expenditure approvals as well as information necessary to establish the reasonableness of expenditure amounts for all future legislative agent or other off-budget expenditures.

Auditee's Response

On the issue of contracting for legislative agent services, The Cooperative's Board of Directors was aware and met with the legislative agent mentioned in the report on several occasions. A vote officially authorizing these services has been taken and completed on the advice of counsel. It is important to note that the Board and the current Chairperson was aware that the monthly costs were \$4,000 per month the first year and about \$3,000 per month the second year. The board voted on Dec. 18, 2009 to approve all past and current contracts with the legislative agent, consistent with their recollections of services rendered by these consultants.

At budget time, we will be reviewing the cost of these services, the nature of these services and the contractor used for these services. At that time we will be making decisions on these matters. However, it is important to note that most towns, cities and school districts rely on membership in various professional organizations to provide legislative agent services. Suburban communities have unique issues and find it necessary to have representation at the State level.

Auditor's Reply

We acknowledge that some school districts rely on membership in various professional organizations to provide legislative agent services. However, our report does not assert that expenditures by school districts or education collaboratives for legislative agent services are inherently improper or unallowable. Rather, our concern is that the legislative expenditures made by TEC during our audit period did not receive prior authorization by the TEC Board of Directors as required by its DESE-approved collaborative agreement. TEC's assertion that its board was aware of the amount of expenditures involved is contrary to statements made to us by TEC's board chairperson, who stated that the board was unaware that payments totaling \$96,000 for legislative agent services through November 25, 2008 had been recorded in TEC's general ledger and that it was her recollection that the board had been led to believe that these expenditures would total only approximately \$20,000. The TEC's board retroactive vote on December 18, 2009 (over two years after the fact) to approve all past and current contracts with the legislative agent does not mitigate the responsibility of TEC's management's staff to obtain prior approval from its board for all agency expenditures including those for legislative agent services. In fact, the TEC collaborative agreement does not provide for the expenditure of

funds on the basis of retroactive approvals, but instead prohibits any expenditure that has not been authorized in advance by the agency's board.

7. IMPROVEMENTS NEEDED IN INTERNAL CONTROLS OVER CERTAIN AGENCY ACTIVITIES

Generally accepted accounting principles (GAAP) require entities such as TEC to establish adequate internal controls over all aspects of their operation. Despite this, we found that during our audit period, TEC had not established adequate internal controls over several aspects of its operation. Specifically, TEC had not taken measures to adequately address all of the internal control deficiencies identified by its private accounting firms during its recent audits, was not making sure it was conducting Criminal Offender Record Information (CORI) checks on certain employees every three years as required by state regulations, did not establish adequate systems to track the time each TEC employee spent working in each activity as required for state and federal accountability purposes, had not established adequate provisions for the return of funds to collaborative members upon their withdrawal from the collaborative, and had not established adequate controls over the use of its telephone systems. These internal control deficiencies can result in a variety of operational and administrative issues, including the potential loss or misuse of agency assets.

GAAP requires that organizations such as TEC establish adequate internal control systems to ensure that goals and objectives are met; resources are used in compliance with laws, regulations, and policies; assets are safeguarded against waste, loss, and misuse; and financial data is maintained, reported, and fairly disclosed in reports. However, during our audit, in addition to those internal control deficiencies detailed throughout this report, we identified the following issues relative to the internal controls TEC had established over certain aspects of its operations:

a. Certain Recommendations on How to Improve Internal Controls Identified during Prior Audits of TEC Were Not Fully Implemented

In the spring of 2007, TEC's Administrator of Finance and Operations found that a TEC employee had apparently misappropriated agency funds. TEC addressed this problem by terminating the individual in question, referring the matter to law enforcement officials, and engaging a private accounting firm to conduct a review of the organization's internal control systems. The accounting firm's review identified various deficiencies, including issues involving control and documentation of food, meeting and travel expenses. For example, the accounting firm stated that, at a minimum, employee reimbursements for all such

expenditures should be accompanied by documentation of the date, duration, place, nature/purpose of the business activity, and the name of the participants. During our audit, TEC officials stated that TEC had addressed its private accounting firms concerns in this area by also having TEC's Treasurer review the documentation prior to payment. However, we found that the Treasurer did not provide an effective control over this activity in that he did not review all transactions, just those over \$250, and he stated that his review was limited to checking documents to see that they had been stamped with the appropriate accounting cost center and expenditure line information and that they had been initialed by TEC's Treasurer. We found that the Treasurer had also apparently approved all submitted transactions, including those where documentation had not met the standards called for by the accounting firm.

During its fiscal year 2008 audit, TEC's private accounting firm reported that approximately 60% of TEC's accounts receivable balance (approximately \$370,000) was over 90 days old, with a substantial amount being over a year old. Of that amount, \$124,552 had been reserved as doubtful to collect. The firm recommended that TEC pursue collection where possible and also make a determination regarding the collectability of items in the reserve. However, during our audit, we found that the reserve accounts receivable items totaled as much as \$30,000 for some TEC member districts and that little progress had been made in resolving these claims. **Although** TEC managers reported that they were continuing to work on addressing this matter, we found that over \$114,000 in accounts receivable remained outstanding in February 2009.

Other identified accounting control deficiencies also remained only partially corrected at the time our audit work was completed, including controls over revenues and expenditures associated with meals prepared by culinary arts classes at TEC's Phoenix School.

b. Personnel Policies and Procedures Such as Criminal Record Checks and Employee Time and Activity Reporting Systems Have Been Inadequate

Massachusetts law makes Criminal Offender Record Information (CORI) maintained by the Commonwealth's Criminal History Systems Board available for certain purposes such as the screening of employees and volunteers. Chapter 71, Section 38R, of the General Laws mandates that this information be obtained for current and prospective employees and volunteers "who may have direct and unmonitored contact with children, including any

individual who regularly provides school related transportation to children.” Information must be updated “periodically, but not less than every 3 years” over the employee’s or volunteer’s period of service. The requirement to conduct CORI checks also applies to contractors where the potential for direct unmonitored contact exists. Although the statute’s language applying these requirements to school committees, superintendents, and principals of public and accredited private schools in the Commonwealth does not expressly reference education collaboratives, DESE officials stated that DESE interprets this law to also apply to education collaboratives. We found that although TEC had completed all of the required initial CORI checks for employees other than the Executive Director, it had only begun, during our audit period, to update its CORI information on its staff at least every three years as required by Chapter 71.

We also determined that TEC’s personnel system fails to use a time and activity reporting system documenting the proportion of time spent by employees on different functions. For example, TEC’s records did not indicate that any of its staff had worked in its cooperative purchasing activity, even though we found that at least three TEC employees devoted a portion of their work time to that activity. We also found that no personnel costs had been recorded for other reporting centers (e.g., the Administrator and Teacher Licensure programs), even where other program and personnel documentation established that employees had been assigned to these programs on at least a part-time basis. In such cases, employee time and associated personnel costs had clearly been incorrectly charged to other programs or to TEC’s management and general administrative activity cost center. In other cases, personnel costs had simply been allocated across multiple activity reporting centers on a predetermined pro-rated basis with no underlying evidence that personnel activity and costs were really the same for each program. As a result of these practices, no accurate record of actual staff resource utilization exists within TEC. This is of particular concern for entities such as TEC, who are typically required by state and federal grants and contracts to accurately document staff work time and associated personnel costs for each grant or contract.

c. Inadequate Provisions Have Been Made for the Return of Funds to Members upon Withdrawal or Termination of the Collaborative Agreement

Chapter 40, Section 4E, of the General Laws requires that the written agreement forming the basis for each collaborative set forth “the method of termination of the education collaborative and of the withdrawal of member school committees.” However, we found that TEC’s written agreement includes only ambiguous provisions providing for distributions to be made in “ratable shares” to member towns “according to funds and other considerations made by each member town.” When we asked about the details of these provisions, the TEC Administrator for Finance and Operations stated that although TEC had financial records dating back to its inception, there were probably multiple reasonable calculation methodologies that could be used and that the members had not agreed upon a specific calculation methodology. In our opinion, the ambiguous language appearing in the TEC collaborative agreement is inadequate and could result in disputes if a member community decides to withdraw from the collaborative.

d. Inadequate Controls over Telephone Usage Resulted in Potential Abuses of TEC’s Telephone System

During our audit, we found that TEC had not established appropriate policies, procedures, or other internal controls relative to the usage of agency telephones. This condition can result in staff using agency phones and associated work time for personal rather than TEC-related activities. In fact, our review of TEC telephone bills during fiscal year 2007 and 2008 documented extensive outgoing long distance calls from TEC phone lines to phone numbers associated with the Executive Director’s consulting firm, its clients, and employment candidates, suggesting that even on days when he was present at TEC, the Executive Director may have been devoting work time for which he was being paid by TEC to his private consulting activities. Yet none of these calls had been tracked by TEC, and TEC had not been reimbursed by the Executive Director or the consulting firm for any private telephone calls and associated employee time. The table below is an example of the telephone calls made from the Executive Director’s telephone during just one month (19 work days) covered by our audit period.

Outgoing Long Distance Calls and Executive Director Activities *
January 5, 2009 through January 30, 2009

Approximate number of apparent non-TEC-related consulting calls	119
Approximate number of apparent TEC-related calls	44
Approximate number of non-TEC-related personal calls (e.g., to out-of-state real estate brokers)	13
Calls for unknown purposes to unidentifiable numbers	<u>40</u>
Total outgoing Verizon Select long-distance calls	<u>216</u>

* Includes out-of-state land-line calls from the TEC central office, but excludes most in-state long-distance calls, which are separately billed, and calls from program site landline phones and cellular phones used by the Executive Director and 12 other TEC managers. Although identified consulting related calls are presumed to have been made by, or at the direction of, the Executive Director, other calls, including those apparently made for personal purposes, may have been placed by other staff at the TEC central office.

Recommendation

TEC should immediately establish an effective system of internal controls over all aspects of its operations and governance activities. Policies and procedures should be documented in writing, approved by TEC's Board of Directors, and distributed to TEC employees.

TEC's board should also consider appointing an audit committee that includes independent external representatives with expertise in finance and financial oversight. Municipal treasurers, accountants, comptrollers or similar staff might be available for this purpose.

Auditee's Response

Regarding Audit Result No. 7a, control issues identified by prior audits, TEC officials stated, in part:

Additional work continues in the area of accounts receivable and additional allowances have been set up. There have been recoveries of accounts that were a few years old. Regarding revenues and expenditures over meals prepared by culinary arts classes, we are unclear about this comment and invite further clarification. But since that time, the receipts and expenditures process has been changed so that the town of Norwood (Senior Center) administers cash receipts and disbursements for this program.

Regarding Audit Result No. 7b, personnel policy, criminal record (CORI) check, and employee time and activity reporting, TEC officials stated, in part:

Our HR Coordinator has set up a database to track CORIs and has created a monthly report. CORIs are done on all prospective employees at the time of hire and then once every three years thereafter. Each staff member is sent a blank CORI form to sign and

return when it is time to re-register that person's CORI. All CORI forms are currently kept on file in the office of the HR Coordinator.

TEC officials did not respond to Audit Result No. 7c regarding collaborative member district withdrawal issues. Moreover, no further response was made to Audit Result No. 7d regarding telephone usage and controls other than the comment provided in response to Audit Result No. 1 that “TEC is currently reviewing issues of time sheets, telephone calls, and vacation time reporting, to help improve our current system, in conjunction with revising the policy and procedure manual.”

Auditor's Reply

In its response, TEC asserts that it is doing additional work in the area of its accounts receivable. However, TEC did not provide us any documentation to substantiate that it has implemented adequate internal controls to address the issue of TEC's overdue or uncollectible accounts receivable amounts. Based on its response, TEC is taking measures to address our concerns relative to CORI records. However, we again recommend that TEC immediately establish an effective system of internal controls over all aspects of its operations and governance activities. Agency policies and procedures should be documented in writing, approved by TEC's Board of Directors, and distributed to TEC employees.

OTHER MATTERS

1. DESE IS NOT EFFECTIVELY MONITORING COLLABORATIVE ACTIVITIES

We found that the Commonwealth's Department of Elementary and Secondary Education (DESE) has not established policies and procedures to effectively monitor the activities of education collaboratives such as TEC. Although DESE has been statutorily assigned certain oversight responsibilities relative to collaborative activities, it has not updated the Education Collaborative Policy that it developed for this purpose since 1988. As a result, this policy is significantly outdated, and many of the oversight provisions detailed in the policy are no longer being implemented. Consequently, DESE does not have effective monitoring, financial reporting, and auditing systems for education collaboratives; does not ensure that a representative from DESE attends and/or participates in each collaborative's board meetings in an advisory capacity as required by state law, and has not adequately addressed issues regarding the applicability of various state laws and regulations that apply to public schools to collaboratives. This condition has resulted in education collaboratives not being held to the same performance standards that apply to public school districts and charter schools within the Commonwealth.

DESE is the Commonwealth's oversight agency for public primary and secondary education and has broad authority and responsibility for activities of school districts, school committees, regional school districts, and alternative education arrangements such as charter schools, approved private special education schools, and education collaboratives. Chapter 40, Section 4E, of the Massachusetts General Laws also gives DESE express control over the provisions of all education collaborative agreements by stating, in part:

The written agreement which shall form the basis of the education collaborative shall set forth the purposes of the program or service, the financial terms and conditions of membership of the education collaborative, the method of termination of the education collaborative and of the withdrawal of member school committees, the procedure for admitting new members and for amending the collaborative agreement, the powers and duties of the board of directors of the education collaborative to operate and manage the education collaborative and any other matter not incompatible with law which the member committees deem advisable. The agreement shall be subject to the approval of the member school committees and the commissioner of education.

In addition, this statute requires that DESE appoint a representative to serve in an advisory capacity (non-voting) to the education collaborative board. Pursuant to its general oversight

responsibilities, DESE (then the Department of Education) promulgated an Education Collaborative Policy (Policy) document in 1977, which was amended in 1988 to reflect provisions of various statutory changes relevant to the operation of education collaboratives.⁸ Despite these statutory provisions and policies, our audit of TEC identified a number of concerns regarding DESE's oversight of TEC and other collaboratives within the Commonwealth, as follows:

a. DESE Has Not Updated Its Education Collaborative Policy Document Since 1988

In order to ensure that its Policy remains current and sufficient for DESE to effect proper oversight of collaborative activities, Section VI of DESE's Policy requires that it be reviewed at least every five years, by stating:

Because of the evolving nature of educational collaboratives, at least every five (5) years the Commissioner of Education [now DESE] will cause this Policy to be reviewed to reflect improvements, areas that need strengthening or changes in legislation. Each Division, Region and program area will participate in this review to assure that the final document accurately reflects the Board of Education's current position with respect to educational collaboratives. This review will be coordinated with representatives of the MA Organization of Education Collaboratives (MOEC).

In addition, the Bureau of School Management Services will coordinate the development of an implementation plan that will provide direction and specific instructions to implement this Policy. The development of this implementation plan will be coordinated with representatives of program area staff within each division of the Department of Education and Regional Education Center with representatives of MOEC and with representatives of affected state and local agencies.

However, during our audit we found that the required five-year reviews and updates of the Policy by DESE have not taken place since 1988. In addition, we found that over the 20 years that have elapsed since the Policy's last update, numerous statutory changes as well as changes in the structure of DESE have rendered much of the references and information in the Policy obsolete. For example, as the result of a restructuring of the Commonwealth's Executive Office of Education and DESE, the Bureau of School Management Services and the Regional Education Centers referenced in the Policy no longer exist. Various education collaborative reporting requirements incorporated into the policy pursuant to Chapter 188 of the Acts of 1985 have also been superseded by more recent education reform initiatives such

⁸ These included Chapter 188 of 1985 (the School Improvement Act) and Chapter 727 of 1987 (An Act Enhancing the Teaching Profession and Recognizing Educational Achievement), and Chapter 631 of the Acts of 1985 (An Act Relative to the Authority of Educational Collaboratives).

as Chapter 71 of the Acts of 1993. As a result, many of the references and requirements in the Policy are outdated, resulting in ineffective internal controls relative to the monitoring of collaborative activities.

b. DESE Has Not Effectively Required Appropriate Auditing, Monitoring, and Financial Reporting for TEC or Other Education Collaboratives

We found that, even if provisions included in the Policy were fully implemented, the adequacy of the Policy's audit and monitoring provisions would be questionable. For example, even though TEC and other education collaboratives within the Commonwealth are multi-million dollar organizations funded annually by public funds, the Policy requires only that a program report and unaudited internally prepared financial statements be submitted by collaboratives to their member school districts on an annual basis and that a copy of the document be sent to DESE every third year. Moreover, a financial statement audit is required only once every three years and then only if the collaborative happens to directly receive at least \$25,000 in grants from DESE. These provisions appear to be inadequate in comparison to current national local governmental and educational agency reporting practices, which typically require audits to be conducted on an annual basis, with annual or even more frequent reporting of performance statistics. TEC's own independent audit firm has also recommended that TEC audits be performed annually.

Chapter 40, Section 4E, of the General Laws requires DESE participation in education collaborative governance activities, stating:

The department of education shall appoint an individual to serve in an advisory capacity to the education collaborative board. Said individual shall not be entitled to vote on any matter, which comes before the board of directors of the education collaborative.

Accordingly, DESE's Policy provides for the appointment of an ex-officio non-voting DESE representative member on each collaborative Board of Directors, as well as annual meetings between DESE and collaborative directors and staff "to discuss regional concerns and to plan and coordinate certain services to local school systems." The Policy also states that DESE "will continue to insure compliance with pertinent program and fiscal requirements by . . . continuing to conduct compliance reviews, program audits and/or program or grant reviews of educational collaboratives in each region." However, our audit found that,

contrary to these oversight provisions, although DESE had nominally designated a central office staff member to represent DESE on TEC's board, the representative has never attended a board meeting and TEC board minutes were not even being sent to the DESE representative. In fact, TEC board representatives stated that, except for the DESE sign-off on annual renewal amendments to the TEC collaborative agreement, they could not recall any board contact whatsoever with DESE, let alone visits or audits by DESE representatives.

DESE currently monitors education collaborative services only in an indirect manner through a Public School Coordinated Review System. This system reviews individual public school districts on a six-year cycle but reviews education collaborative services to a district only where the collaborative happens to serve one or more students who are included in the student record sample selected by DESE for review or where a collaborative operated classroom exists in a public school and has been selected for inclusion in the DESE review being conducted for that particular school district. Even if one of the sampled students is served by a collaborative or a collaborative classroom is selected for inclusion in the review, only the records and services for that particular student or classroom are reviewed - not the activities of the collaborative as a whole. Although additional school-specific reviews may also be performed every few years for collaborative-operated alternative schools such as the two run by TEC, those reviews are not comprehensive reviews of collaborative operations as a whole, but instead focus only on the activity of the individual school. In fact, during our meetings with DESE officials, these officials stated that aside from annual sign-offs on collaborative agreement amendments and the extremely limited and infrequent program review activity described above, DESE is no longer performing activities called for by the Policy. Instead, DESE officials stated that they rely on school committees and their superintendents to provide oversight of education collaboratives in which they are members.

In our opinion, these oversight arrangements are inadequate and, in the case of a DESE representative serving in on each collaborative's board in an advisory capacity, not in compliance with the above cited statutory and policy requirements. We also noted that a January 2009 report issued by the Massachusetts Organization of Educational Collaboratives on educational service agencies in Massachusetts includes the following language characterizing the state of accountability arrangements for education collaboratives in Massachusetts:

*Currently, there is no consistent system of accountability for Massachusetts Collaboratives other than the requirements of specific grantors and broad membership. Given the loosely defined structures of Massachusetts Collaboratives, some engagement by SEA [DESE] officials in ongoing benchmarking exercises, setting criteria, and evaluation of cost-sharing programs is essential.*⁹

c. The Special Legal Status of Massachusetts Education Collaboratives Raises Issues Regarding the Applicability of State Laws and Regulations That DESE Has Not Adequately Addressed

When education collaboratives were first established under Chapter 40, Section 4E, of the General Laws, employee collective bargaining issues arose resulting in a legal determination by the Massachusetts Labor Commission (MLC – now the Massachusetts Labor Relations Commission) in 1980, that collaboratives were non-independent joint enterprises of school districts offering educational programs and services that were an essential part of the school’s normal operations and that collaboratives were therefore subject to the Commonwealth’s collective bargaining laws. This 1980 determination by MLC stated, in part:

*To rule otherwise would be to allow school systems to provide usual and legally-mandated services while avoiding responsibilities under the Law, which is designed to provide collective bargaining rights to all public employees, including employees of school systems.*¹⁰

However, during our audit, a member of DESE’s legal staff advised us that, due to a 1985 language change to Chapter 40, Section 4E, education collaboratives now have independent legal status and that, in the DESE’s opinion, they are no longer subject to various Massachusetts education laws and regulations governing school districts and school committees. In addition to the exemptions to DESE’s licensure requirements previously discussed, we identified issues regarding the applicability of other provisions of Massachusetts laws and regulations to education collaboratives. These cover a wide array of provisions ranging from teacher tenure, suspension, and disciplinary rights to various key statutory requirements such as the provisions in Chapter 71, Section 37L, of the General Laws applicable to the handling and reporting of instances of child abuse and neglect and weapons violations, which apply to public schools directly operated by school committees. During our audit, we spoke with TEC officials about this matter, but they were unable to

⁹ <http://moecnet.org/wp-content/uploads/2008/05/esasinma-moec-jan2009-1.pdf> In the report, which uses national educational terminology, “SEA” stands for “State Educational Agency” – the general term covering state departments of education such as DESE.

¹⁰ SHORE COLLABORATIVE and MASSACHUSETTS FEDERATION OF TEACHERS, Case No. MCR-2894, October 7, 1980, 7 MLC 1351

provide us with any clarification regarding the applicability of various education laws and regulations to its operations. These officials stated that although DESE had provided some case-by-case verbal guidance, it had not provided any formal written.

We then asked DESE officials about the applicability of various statutes and regulations that apply to all public schools within the Commonwealth to education collaboratives. In response, these officials stated that since education collaboratives are free-standing legal entities, in these officials' opinion, they are generally not subject to the provisions of the Massachusetts Special Education Law (Chapter 71). However, in a June 11, 2009 e-mail a member of DESE's legal counsel stated, in part:

It should be noted that there are instances where the Department has determined that certain statutory provisions apply to collaboratives, notwithstanding the fact that such provisions do not specifically apply to collaboratives. For example, G.L. c. 71, § 38R, the law that requires all schools to conduct criminal background checks on current and prospective employees and volunteers, including those who regularly provide school related transportation to students, who may have direct and unmonitored contact with children. While certain educational entities, such as educational collaboratives, are not expressly covered by the statute, the Department has interpreted the law to apply to all K-12 public and private schools, public school districts, educational collaboratives, charter schools, approved day and residential special education schools, and private providers of educational services for children with which a local education agency has contracted.

Additionally, the Department considers collaboratives to be a school committee, school district, or public school for certain specific purposes. The following regulations contain provisions whereby collaboratives are considered to either be a school committee, school district, or public school for the purposes of such regulations:

603 CMR 4.00, Vocational Education (school committee)

603 CMR 14.00, Education of English Language Learners (school district)

603 CMR 18.00, Program and Safety Standards for Approved Public or Private Day and Residential Special Education School Programs (approved public special education school)

603 CMR 23.00, Student Records (school committee)

603 CMR 28.00, Special Education (approved public special education school)

603 CMR 30.00, Massachusetts Comprehensive Assessment System And Standards For Competency Determination (school committee)

603 CMR 35.00, Evaluation of Teachers and Administrators (school committee)

603 CMR, 46.00, Physical Restraint (publicly funded education program)

The attorney also wrote:

Chapter 71 contains approximately ninety sections, most of which specifically apply to school committees, school districts and public schools. In order to provide you with a comprehensive list of which provisions of Chapter 71 apply to collaboratives, I would have to conduct a thorough review of all the sections contained in Chapter 71, with an eye to determining which ones are applicable to education collaboratives. In the absence of such a massive undertaking, it is not possible for me to provide you with an exhaustive list of which provisions of Chapter 71 apply to education collaboratives.

In the same communication, DESE responded to our inquiry as to whether DESE had issued any guidelines regarding other specific local government legal requirements such as conflict-of-interest laws and prohibitions on charging service fees in excess of anticipated actual direct and indirect costs to collaborative. DESE stated that it had not done so and added, “Since the member school committees are represented on the board of directors by either a school committee member or the superintendent, the expectation is that the board of directors are cognizant of the law.”

In our opinion, since DESE has not yet itself determined what aspects of the various laws and regulations that apply to public schools within the Commonwealth apply to collaboratives, it may be unreasonable for DESE to assume that superintendents and school committees are making these determinations in an accurate manner.

An example of the problems raised by these uncertainties involves the issue of various reporting requirements. In the past, collaboratives were required by law to comply with educational reporting provisions established by Chapter 188 of the Acts of 1985 for all public schools and education collaboratives, including submission of a “Collaborative Report” that disclosed program, staff, facility, prototype, and service information comparable to the information gathered from public school districts. However, more recent educational reform statutes have superseded the Chapter 188 reporting provisions without expressly applying new statutory provisions to collaboratives. As a result, when new statewide school district reporting requirements such as DESE’s Education Personnel Information Management System (EPIMS) have been implemented in recent years, they have not been required for education collaboratives even though DESE designed the new systems to facilitate compliance with state and federal reporting requirements. EPIMS is also linked to DESE’s

separate data system on educator licensure, enabling DESE to verify educator licensure and qualification representations made by school systems. However, the reporting requirements legally apply only to other educational settings such as local school districts, regional school districts, and charter schools, not to education collaboratives. As a result, DESE does not have important information regarding collaborative employees and has no practical means of detecting instances in which TEC or other collaboratives are not in compliance with applicable licensure requirements. This reporting approach creates a significant risk that TEC and possibly other education collaboratives might be substantially out of compliance with DESE licensure requirements for an extended multi-year period without DESE detecting or addressing this noncompliance.

Recommendation

DESE should immediately update its Policy and implement effective monitoring and oversight arrangements. To the extent that additional statutory language may be required to ensure that DESE has authority to regulate collaborative personnel and activities, DESE should propose appropriate statutory amendments similar to provisions in place for regional school districts and charter schools. For example, Chapter 71, Section 89, of the General Laws states that “A charter school shall operate in accordance with its charter and the provisions of law regulating other public schools” and expressly identifies the limited exceptions in which charter schools are appropriately not to be subject to the same requirements as other public schools. The inclusion of similar language in Chapter 40, Section 4E, of the General Laws might resolve existing uncertainties regarding DESE’s authority to appropriately regulate and oversee the activities of education collaboratives.

DESE Comments

DESE’s Commissioner provided the following comments:

I concur with the recommendation that the Department needs to update its twenty-two year old policy on collaboratives and, as part of that update, we need to address the frequently-asked questions on what provisions of state education law do, and what provisions do not, apply to these organizations. As noted in your report, our existing policy pre-dates the Commonwealth’s 1993 education reform law. Much has changed in the intervening years, including the roles of collaboratives themselves, and so a fresh review of these issues is indeed overdue. I intend to carry out this review during the coming calendar year and have asked . . . in our school governance office to lead this

effort. She will coordinate our internal review as well as manage outreach to the educational collaboratives and other constituent agencies.

As part of this review, we will address the appropriate mechanisms for ongoing state oversight of collaboratives. In so doing, we will need to find a workable framework that will safeguard the public interest and that can be accomplished within the limited resources available to us.

As you suggest, we may determine during the course of this review that statutory changes are required to provide needed clarity on certain issues. Also, we will consider the option of issuing regulations in addition to an updated policy. During the course of our review, we intend to consult with local officials, including those from school districts and from the collaboratives themselves, as well as the various state oversight agencies that may have some role to play. I hope you will allow us to seek advice from your office on key issues...

2. COLLECTIVE PURCHASING ACTIVITIES COULD BE IMPROVED THROUGH CONSULTATION WITH THE OPERATIONAL SERVICES DIVISION AND THE OFFICE OF THE INSPECTOR GENERAL

TEC conducts collective purchasing of school, cafeteria, custodial, and athletic supplies, as well as fuel and natural gas, on behalf of as many as 60 Massachusetts school districts. Our audit indicated that these collective purchasing services appear to generate significant benefits and savings for participating districts. However, we believe that TEC should further consult and coordinate its procurement activities with the Commonwealth's Operational Services Division (OSD), which conducts similar statewide procurements open to participation by state and local government, and with the Office of the Inspector General (OIG), which oversees local government purchasing activities.

School districts in Massachusetts have essentially four options for purchasing goods and services:

- 1) They can procure them through their own internal purchasing systems, which allows a district full control over procurement but can be administratively burdensome and may fail to realize savings that are available through larger scale bulk purchasing systems.
- 2) Where a city or town has established a central purchasing office, that office may conduct procurement activity on behalf of the community's school district.
- 3) Local governmental entities such as municipalities, school districts, and education collaboratives may purchase certain goods and services through statewide contracts developed by the OSD for a variety of commonly purchased items such as office equipment and supplies, fuel and utilities, food, computers and IT services, etc. Statewide contracts are developed through a public bid process conducted by state employees with extensive purchasing expertise and purchases are generally designed to realize economy and efficiency

benefits available through large scale bulk purchasing. State agencies participate on a mandatory basis, while local governmental agencies participate on a voluntary basis.

- 4) Alternatively, Chapter 7, Section 22B, of the General Laws authorizes local governmental entities to conduct “collective purchasing” of goods and services. Under these arrangements, a single local governmental entity conducts procurement activities on behalf of a pre-identified group of other local governmental entities for specific goods or services. This arrangement allows participants to realize economy and efficiency benefits similar to those provided by the OSD system but with greater flexibility to address the individual needs and desires of participants.

TEC operates a collective purchasing program, which it refers to as “cooperative purchasing,” and annually conducts six public bid solicitations for paper, office, classroom, art, and computer supplies; food services (groceries, milk, bread, etc., but not cafeteria “food service” operations); athletic equipment and supplies; custodial supplies; fuel oil; and natural gas. These collective procurements are conducted not just for TEC and its 16 member districts, but also on behalf of non-member school districts. Participation and expenditures vary for each bid category. Almost 60 districts participate in TEC’s bid for paper, office, classroom, art, and computer supplies totaling approximately \$5 million per year in purchases, whereas fewer districts participate in other procurements (e.g., 21 districts with a purchasing total of under \$200,000 for athletic equipment and supplies, and just nine districts for natural gas). On a consolidated basis, procurement volume exceeds \$6 million per year. Except for certain budgeting, accounting, and expenditure issues discussed in our Audit Results section of this report, we found TEC’s collective purchasing services to be well run and effective, realizing significant cost savings on behalf of participating districts.

The collective purchasing program at TEC is operated on a part-time basis with staff who have been trained and certified through the Massachusetts Certified Public Purchasing Official (MCPPO) program operated by the OIG, which provides certain oversight of local government procurement activities, including capacity building training and educational activities designed to promote procurement quality, integrity, and compliance with procurement laws such as Chapter 30B of the General Laws. TEC procurement activity is spread across the school year from September through June, with bid opening dates generally occurring from late February through April. Participation is open to any Massachusetts school district, so long as the district signs up for the selected bid by the specified bid development cut-off date. This is required for compliance with the provisions of Chapter 7, Section 22B of the General Laws, Collective

Purchasing by Political Subdivisions, which, unlike OSD statewide contract open participation terms, effectively require that all participating public purchasers be pre-identified prior to issuance of the bid. The statute reads:

Notwithstanding any contrary provision of law relating to collective purchasing, but subject, however, to all other laws regulating public purchases and competitive bidding, any two or more political subdivisions, as defined in section twenty-two A, may join together for the purpose of obtaining and accepting competitive bids on similar items of materials, supplies, equipment or services which they intend to purchase, provided that each political subdivision shall accept sole responsibility for any payment due the vendor for its share of such purchase. No political subdivision which serves as a purchasing agent under the provisions of this section shall be liable solely by reason of its actions as such agent for any claim based upon a breach of warranty or defects in the design, manufacture or installation of the materials, supplies or equipment purchased pursuant to this section.

TEC member districts participate without charge, whereas non-member districts are required to pay per-procurement participation fees that vary for each procurement type, running as high as \$550 per purchasing district for the school and food supply procurements.¹¹ Bidders are also charged minimal bid-package pick-up fees of approximately \$30, which are imposed for the purpose of discouraging document requests from parties other than committed bidders.

TEC has represented to participating school districts, and to other interested parties such as legislators, that the collective purchasing operation has generated lower prices and significant savings compared to those available at market price or through other procurement arrangements such as the OSD statewide contract system. The collective purchasing system also allows school districts to realize administrative savings by reducing the need for freestanding internal bid administration systems at each district. Although we did not verify the dollar amount of savings as represented by TEC (e.g., \$1.75 million on classroom supplies and \$220,000 on dairy products), we reviewed the general accuracy of these representations and the asserted merits of the system with largely positive results, but found the presented savings amounts to be simply very rough estimates rather than carefully tracked or projected savings amounts.

We were able to confirm for various items we tested in the office and school supply, athletic equipment, and food and custodial procurement categories that prices were typically as low as or lower than available through OSD statewide contracts, which other studies have found to be

¹¹ As described in Audit Results No. 2 on budgeting and pricing issues, the participation fees established by TEC have been designed to generate a profit to benefit TEC members and appear to be in conflict with restrictions limiting fee amounts to anticipated actual direct and indirect costs of conducting these activities.

typically lower than market rates. These savings may perhaps be due at least in part to the fact that TEC cooperative purchases lock in participation and purchase volume levels in advance rather than allowing, as the OSD statewide contract system does, participation by public purchasing entities on an open-ended basis with no guarantees to bidders regarding purchase volume level.

We also identified a potential compliance issue for OSD statewide contracts associated with this lack of coordination. Although TEC sometimes establishes contracts for similar or identical items available through the statewide contract system, but with different vendors, TEC also often procures the same items from the same vendors providing the items under statewide contracts. Examples we noted included the purchase of certain identical dairy products and baked goods from the same suppliers under both the TEC and OSD statewide contract procurements, but at different prices, as shown in the table below:

**Same Item/Same Supplier Price Variances for TEC and OSD Statewide Contract Procurements
(Fiscal Year 2009 prices)**

Comparison Item Examples	Percent TEC Price Was Lower than Statewide Contract Price for Same Item from Same Supplier
Baked Goods - three items (Bread, Rolls, etc.)	2.4% to 18.8% lower, depending on item
Eight-Ounce Milk Products - four items (Skim, 1%, Chocolate, Strawberry) priced by four school district location regions for TEC and at a single per-item price for the Statewide Contract	12.0% to 26.4% lower, depending on item and region

According to the OIG, the OSD's statewide contract provisions have been interpreted to mandate that in cases where statewide contract vendors offer a lower price to other public purchasers, including those participating in collective purchasing programs, the same lower prices must then be passed on to all governmental purchasers in the state-wide contracting system. Despite the price variances we identified during our testing such as those summarized in the above table, we saw no evidence in published statewide contract documents that the suppliers had passed price reductions for these items through to statewide contract purchasers as required by OSD. Although it is not TEC's responsibility to enforce compliance with OSD statewide contract pricing provisions, this compliance issue has obvious implications for TEC and its vendors as well as for statewide contract participants, since monitoring compliance and

the complexities of resolving errors or settlement disputes can create problems for all parties. Given the difficulties involved in calculating adjustments involving differences in pricing and delivery terms (e.g., delivery to loading dock or to office/kitchen space) that can exist between the two procurement systems and the burdens on vendors of tracking compliance with the OSD price reduction requirement, it is reasonable to expect that at least some vendors can be expected to forgo participation in one or the other of the two procurement systems in order to minimize the potential for being cited as noncompliant. As collective purchasing systems operated by TEC and other local governmental entities continue to expand, such problems are likely to intensify.

Recommendation

The OSD, the OIG, TEC, and other collective purchasing groups active in the Commonwealth should improve their coordination to address this issue in a manner that could reduce compliance issues with benefits for all involved.

TEC's Comments

TEC provided the following comments:

We have always followed DESE's guidelines and will continue to do so in the future.

TEC provides joint purchasing for 90 school districts and towns within the Commonwealth. We save these communities significant dollars on a wide range of goods and services as documented in your report. We are more than willing to share our vendor lists and prices with any interested parties at the State level.

APPENDIX

The Education Cooperative Governance

Fiscal Year 2009

School District	TEC Board Member *	Superintendent
Canton Public School District	Mr. Tim Brooks	Dr. John P. D'Auria
Dedham Public School District	Ms. Tracy Driscoll	Ms. June Doe
Dover Public School District	Ms. Jennifer DaSilva	Ms. Valerie Spriggs **
Sherborn Public School District	Ms. Heather Peck	Ms. Valerie Spriggs **
Dover-Sherborn Regional School District	Ms. Rainie Pearson	Ms. Valerie Spriggs **
Framingham Public School District	Ms. Beverly Hugo (Secretary)	Dr. Eugene Thayer
Holliston Public School District	Ms. Virginia Murphy	Mr. Bradford Jackson
Hopkinton Public School District	Ms. Rebecca Robak	Dr. John Phelan, Jr.
Medfield Public School District	Ms. Debra Noschese	Mr. Robert C. Maguire
Natick Public School District	Ms. Karen Adelman Foster *** Ms. Anne Blanchard ***	Dr. Peter Sanchioni
Needham Public School District	Dr. Donald Gratz (Vice-Chair)	Dr. Daniel Gutekanst
Norwood Public School District	Mr. Mark Joseph *** Mr. Mitch Pentowski ***	Mr. John Moretti
Walpole Public School District	Ms. Nancy Gallivan	Mr. Lincoln D. Lynch III
Wayland Public School District	Mrs. Heather A. Pineault *** Ms. Deborah Cohen (Alternate Member) ***	Dr. Gary A. Burton
Wellesley Public School District	Ms. Suzi Newman	Ms. Bella Wong
Westwood Public School District	Ms. Barbara Delise (Chair)	Mr. John Antonucci

Others:

Mr. Robert Hilliard, Treasurer appointed by TEC Board of Directors
 Dr. John P. Connolly, TEC Executive Director
 Ms. Nancy Sullivan, TEC Assistant Executive Director
 Mrs. Gail Ross-McBride, TEC Administrator of Instructional Services
 Ms. Deborah H. Brown, TEC Administrator of Operations and Finance
 Ms. Karen DeCoster, Massachusetts DESE designated ex officio member of TEC Board of Directors

Notes:

* All listed members of the Board of Directors were identified by TEC as School Committee members of their respective school districts.

** The Dover Public School District, Sherborn Public School District, and Dover-Sherborn Regional School District, although legally separate districts, employ a single Superintendent.

*** TEC identified two individuals each from the Natick, Norwood, and Wayland school committees as members of the Board of Directors despite the fact that the TEC collaborative member agreement permits only a single member of the Board of Directors for each member school district. For Wayland, one of the two members is identified as an Alternate.