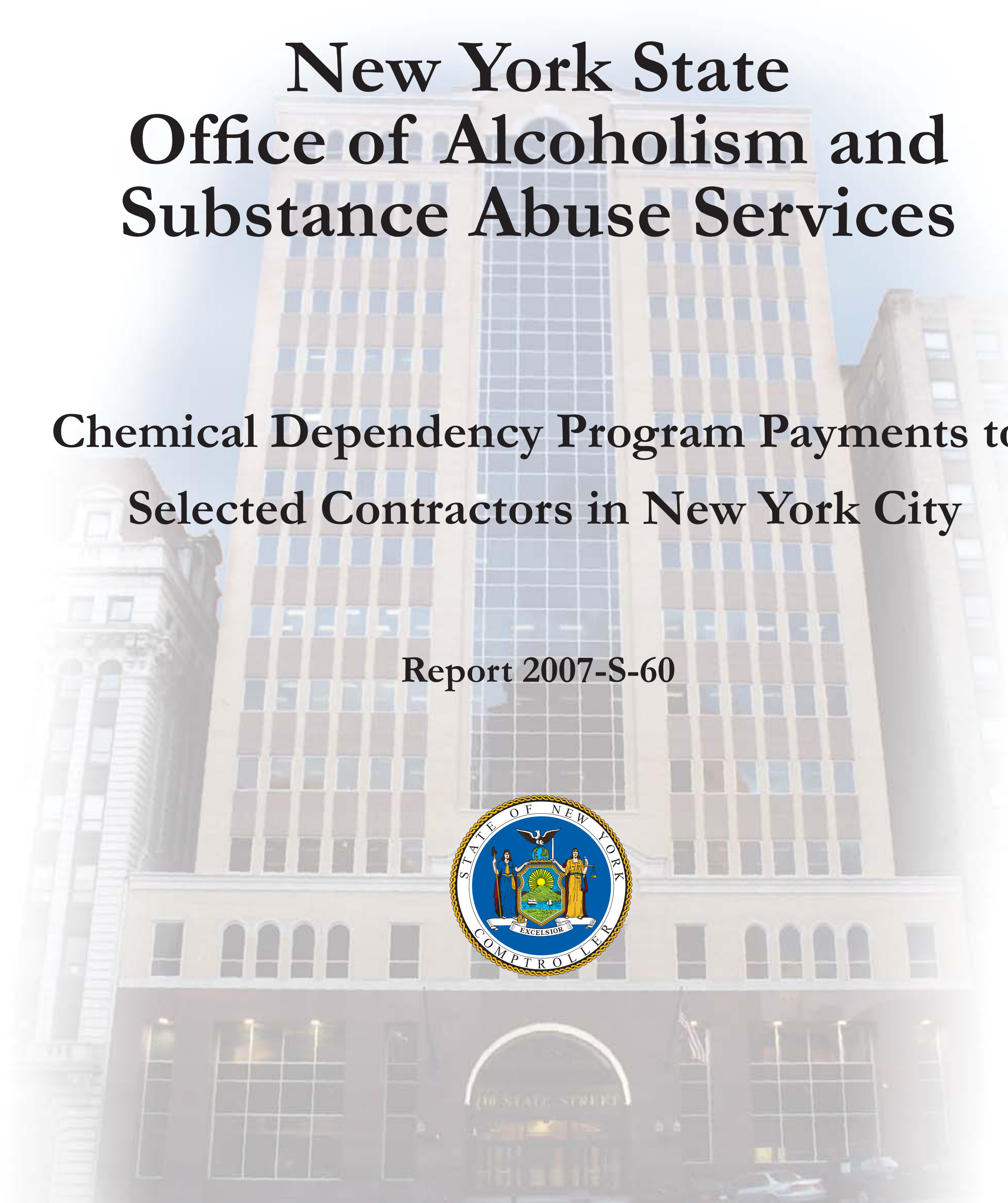
OFFICE OF THE NEW YORK STATE COMPTROLLER

DIVISION OF STATE GOVERNMENT ACCOUNTABILITY

New York State Office of Alcoholism and Substance Abuse Services



Chemical Dependency Program Payments to Selected Contractors in New York City

Report 2007-S-60

Thomas P. DiNapoli

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State of New York
Office of the State Comptroller

Division of State Government Accountability

May 6, 2010

Ms. Karen M. Carpenter-Palumbo
Commissioner
Office of Alcoholism and Substance Abuse Services
1450 Western Avenue
Albany, NY 12203

Dear Ms. Carpenter-Palumbo:

The Office of the State Comptroller is committed to helping State agencies, public authorities and local government agencies manage government resources efficiently and effectively and, by so doing, providing accountability for tax dollars spent to support government operations.

The Comptroller oversees the fiscal affairs of State agencies, public authorities and local government agencies, as well as their compliance with relevant statutes and their observance of good business practices. This fiscal oversight is accomplished, in part, through our audits, which identify opportunities for improving operations. Audits can also identify strategies for reducing costs and strengthening controls that are intended to safeguard assets.

Following is a report of our audit of the Office of Alcoholism and Substance Abuse Services, entitled Chemical Dependency Program Payments to Selected Contractors in New York City. This audit was performed pursuant to the State Comptroller's authority under Article V, Section 1 of the State Constitution and Article II, Section 8 of the State Finance Law.

This audit's results and recommendations are resources for you to use in effectively managing your operations and in meeting the expectations of taxpayers. If you have any questions about this report, please feel free to contact us.

Respectfully submitted,

Office of the State Comptroller
Division of State Government Accountability

State of New York
Office of the State Comptroller

EXECUTIVE SUMMARY

Audit Objective

The objective of our audit was to determine whether payments made by the Office of Alcoholism and Substance Abuse Services (OASAS) to selected Chemical Dependency Program contractors were appropriate and adequately supported.

Audit Results-Summary

OASAS oversees the nation's largest and most diverse system of prevention, treatment and recovery services for drug and alcohol addiction. On July 1, 2004, OASAS entered into one five year contract with Palladia, Inc. (Palladia), and another with Queens Child Guidance Center (Guidance Center), to provide a range of chemical dependency treatment and program support services (Program). Besides their State funding, contractors collect revenues from several other sources including Medicaid and private insurance companies. OASAS' contracts cover Program related expenses that exceed Program related revenues from other sources (net deficit funding), up to the amount of the contract.

For the year ended June 30, 2006, OASAS paid Palladia $8.03 million, and the Guidance Center $346,223, which were the approved contract amounts. During this same period, the two contractors reported approximately $15.2 million in Program-related expenditures (Palladia reported $14.6 million and the Guidance Center reported $603,143). Based on the dollar value of the associated claims, we judgmentally selected for review $11.8 million of these reported expenditures including direct expenses (e.g., payroll) and indirect expenses (administrative expenses) reported by these contractors.

We found that Palladia and the Guidance Center could not adequately support the $8.4 million they received from the State. Both did not fully comply with their OASAS contract requirements, and Palladia also failed to comply with federal regulations. As a result, we could not verify that most of their Program-related expenditures were for State contract-funded programs. Since the total amounts of unsupported Program-related expenditures exceeded the total amount the contractors were actually paid by OASAS, if no additional support surfaces, we recommend OASAS recover all State funds paid to these contractors ($8 million to Palladia and $346,223 to the Guidance Center), unless follow-up audit for subsequent program assessment by OASAS verifies that certain of these costs were appropriate despite the absence of an appropriate allocation methodology.

For employees who work on multiple programs, contractors must maintain specific evidence to justify how they allocated employee direct time among the programs. We found neither contractor could fully show how Program-related salaries or other expenditures were allocated among the programs they operate. We determined that some expenses charged to the State-funded contracts were for programs not covered by the State contracts. For example, 5 of 14 Palladia employees we interviewed indicated that they worked on several programs including some not funded by the State contracts. However, their salaries were not allocated and were charged in full to the State contracts.

In general, contractors are required to allocate the administrative expenses they incur to all their programs based on the ratio of each program's operating cost to total operating expenses. Since we could not confirm that operating costs incurred, such as payroll, were accurate and appropriate, we also could not verify that Palladia and the Guidance Center appropriately allocated administrative costs. We did, however, review the process that both contractors used for allocating administrative expenses and found that neither used the above-noted method for allocating administrative expenses, or any other OASAS-approved methodology.

Contractors are also required to allocate rent and related expenses (e.g., utilities, repairs, maintenance and depreciation) they incur for programs that share the same geographic location, among all programs that benefit from those resources. We found that the Guidance Center did not allocate rent expenses appropriately. For example, the Guidance Center operates four Programs at one location, two of which were funded by the OASAS contract. The two largest rooms at this location were charged only to the OASAS contract. We found, however, these rooms were used by a non-State funded contract program, as well. Since the Guidance Center's related expenses were allocated based on the rent allocation, which we found to be incorrect, the related expense allocation is also not appropriate. We found that Palladia also did not have adequate support for its related expenses.

We also found that OASAS did not effectively monitor contractor operations to ensure it only funds actual program deficits.

Our audit report contains seven recommendations to improve OASAS' controls over Program contracts. OASAS officials generally agree with our recommendations but believe some of our narrative and recommendations overstate the nature of concerns or call for recoveries beyond conditions and/or costs that were questioned.

Auditors' Comments: We believe our findings and recommendations are accurate. Moreover, we note that OASAS stated that it has initiated on-site follow-up audits at Palladia and Queens Child Guidance Center that will identify specific recoveries for charges that could not be supported or documented as program-related.

This report, dated May 6, 2010, is available on our website at: http://www.osc.state.ny.us.
Add or update your mailing list address by contacting us at: (518) 474-3271 or
Office of the State Comptroller
Division of State Government Accountability
110 State Street, 11th Floor
Albany, NY 12236

Introduction

Background

The New York State Office of Alcoholism and Substance Abuse Services (OASAS) oversees the nation's largest and most diverse addiction system. Its mission is to improve the lives of New Yorkers by leading a premier system of addiction prevention, treatment and recovery services. OASAS licenses, inspects, monitors and funds more than 1,300 local chemical dependence treatment programs.

In our prior audit of child care-related grants awarded by the New York State Office of Children and Family Services (OCFS) to a sample of New York City-based child care centers (Audit Report 2006-S-33, released July 2, 2008), we found systemic abuse of those grant monies by center personnel. Based on this audit, we concluded there is a risk that centers that received a child care-related grant may also have inappropriately used other State funds they received. We therefore identified four providers that received reimbursements from both the OCFS and OASAS. We judgmentally selected two of these, Palladia Inc. (Palladia), based on the dollar amount of grants it had received, and Queens Child Guidance Center (Guidance Center), based on the risks we identified during our prior OCFS audit, for further review.

On July 1, 2004, OASAS entered into a five-year State-funded contract with Palladia, and a five-year State-funded contract with the Guidance Center. The contracts require Palladia and the Guidance Center to provide chemical dependency treatment and program support services (Program). The Program provides medical supervision and rehabilitation services to outpatients and intensive residential supervision. Palladia operates 29 distinct human service programs in New York City, eight of which are included in the State-funded contract we reviewed. The Guidance Center operates 11 therapeutic sites, three of which are included in the State-funded contract we reviewed.

The contractors are required to pursue, collect and report all revenue and expenditures relating to the Program. The revenue must be used to pay for Program-related expenditures. The State-funded contracts are net deficit funded which means that if approved Program-related expenditures exceed the amount of non-State Program-related revenue collected, then OASAS will pay the difference up to the contract amount for the year. If revenue exceeds expenditures, OASAS does not pay anything to the contractors.

OASAS approves each contractor's annual budgets, which outline estimated Program-related expenditures and anticipated revenues, program workscopes, and services to be provided. OASAS has the right to modify the submitted budgets, with limitations, throughout the year to reflect Program changes. The Program contracts require documentation for all expenses and revenue collected relating to the contract to be retained for six years from the time the final contract payment is made.

Contractors are also required to adhere to the policies and procedures contained in the New York State Consolidated Fiscal Reporting and Claiming Manual (Manual). The Manual requires contractors to submit periodic fiscal reports to OASAS. These reports include a Consolidated Quarterly Report (CQR), and a Consolidated Fiscal Report (CFR), which is submitted annually and is used as the basis for reimbursement. Both reports detail expenditures and revenue collected for each program funded by OASAS' State-funded contracts. These reports detail expenditures by categories (e.g., Personal Service Expenses, Administrative Expenses, Other then Personal Service, etc.). Within each of these categories, the contractors must denote the portion of expenditures and revenues allocated to each of the State-funded contract programs and document the time and effort of shared staff between different programs using an acceptable basis of allocation or time studies.

Our audit focused on the expenditures charged to the State-funded contracts.

In addition to State funds, OASAS receives Federal funds from a block grant. OASAS allocated $2.3 million of these Federal funds to Palladia for the Program as part of its State-funded contract. Since Palladia received some Federal funding it is required to adhere to federal regulations and Federal Circular A-122 (Circular). The Circular establishes principles for determining costs of grants and contracts for non-profit organizations. The Circular prohibits the use of budget estimates (e.g., estimating which projects employees will work on at the beginning of the year instead of reporting actual work efforts) to allocate expenditures such as payroll and administrative costs.

According to the contracts, Palladia's maximum contract value was $43.6 million and the Guidance Center was approximately $1.9 million. For the period July 1, 2005 through June 30, 2006, Palladia received $8,032,665 ($8 million) from its State-funded contract with OASAS and the Guidance Center received $346,223. Further, for the year ending June 30, 2006, the Guidance Center reported that it collected $75,087 and Palladia reported that it collected $1.45 million in Medicaid revenue.

Audit Scope and Methodology

We audited OASAS payments to selected providers for the period August 3, 2005 through August 9, 2007.

To accomplish our objective, we reviewed applicable laws, regulations, policies, procedures and contracts. We conducted site visits to providers and interviewed OASAS and contractor officials. For each contractor, we reviewed the general ledgers specific to the OASAS contract and compared the totals to those reported in the CFR. We reviewed available documentation for personal service expenses (payroll), administrative expenses, and rent and related expenses for Palladia and the Guidance Center for the year ending June 30, 2006. These expenditures were selected based on their dollar value.

We contacted vendors that the contractors claimed they purchased items or services from, to confirm that such items or services were provided and vendors received reported payments. Additionally, we reviewed leases and allocation methodologies for personal services, administrative costs and rent. For both contractors we also obtained a listing of Medicaid payments received, by location, from the Department of Health to verify revenue reported was reasonably accurate.

We conducted our performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

In addition to being the State Auditor, the Comptroller performs certain other constitutionally and statutorily mandated duties as the chief fiscal officer of New York State. These include operating the State's accounting system; preparing the State's financial statements; and approving State contracts, refunds, and other payments. In addition, the Comptroller appoints members to certain boards, commissions and public authorities, some of whom have minority voting rights. These duties may be considered management functions for purposes of evaluating organizational independence under generally accepted government auditing standards. In our opinion, these functions do not affect our ability to conduct independent audits of program performance.

Authority

The audit was performed pursuant to the State Comptroller's authority as set forth in Article V, Section 1 of the State Constitution and Article II, Section 8 of the State Finance Law.

Reporting Requirements

A draft copy of this report was provided to OASAS officials for comment. Their comments were considered in preparing this final audit report. Their comments along with rejoining State Comptroller's Comments are included at the end of this report.

Within 90 days of the issuance of this final report, in accordance with Section 170 of the Executive Law, the Commissioner of OASAS shall report to the Governor, the State Comptroller and leaders of the Legislature and fiscal committees, indicating the steps OASAS has taken to implement our report recommendations, and where they have not been implemented, the reasons therefor.

Contributors to the Report

Major contributors to this report include William Challice, Frank Patone, Richard Sturm, Donald Geary, Randy Partridge, Vicki Wilkins, Nicholas Angel, Nancy Shrader and Sue Gold.

Audit Findings and Recommendations

According to their State-funded contracts, Palladia and the Guidance Center could only receive State funds, up to the contract amount, if their Program-related expenditures exceeded all non-State Program-related revenue collected. For the fiscal year ending June 30, 2006, Palladia reported $6.1 million in revenue and $14.6 million in expenditures. As a result, Palladia received the maximum amount allowed ($8.03 million) from OASAS. For the same period, the Guidance Center reported $256,920 in revenue and $603,143 in expenditures, resulting in $346,223 in funding from OASAS.

We reviewed support documentation relating to payroll, administrative expenses and rent and related expenses for Palladia and the Guidance Center for the year ending June 30, 2006. In total, we reviewed approximately $11.8 million in Program-related expenditures. We found that the contractors could not adequately support these Program-related expenses and we could not verify that most of these expenditures were for State contract-funded programs. We recommend OASAS recover all of the State funds paid to these contractors ($8.03 million to Palladia and $346,223 to the Guidance Center) for this period unless it can be determined the expenditures were for State contract-funded programs.

Expenditures

Payroll Expenses

According to the Manual, contractor salaries must be reported in the CFR by program. If employees worked on more than one program, contractors must allocate the salaries to the various programs based on the actual time and attendance devoted to each program. If salary expenses are allocated based on a time study, instead of actual efforts, the study must be performed quarterly and it must include an analysis of the employee's time and effort for at least a two week period. If employees work on programs that are both part of State-funded contract and non-State funded contract programs, only that portion of work done on the State-funded contract is to be reported as a Program expenditure. The Circular also requires Palladia to use and retain reports that reflect an after-the-fact allocation of an employee's salary. This allocation must be based on actual work efforts and cannot be based on estimates.

Of the $11.8 million in Program-related expenditures we reviewed, approximately $8.3 million was payroll related ($7.9 million for Palladia and $406,058 for the Guidance Center). We reviewed payroll records and the CFRs for both contractors for the year ending June 30, 2006. We found that neither Palladia nor the Guidance Center allocated payroll costs in accordance with the Manual, and Palladia also did not allocate payroll or maintain payroll records in accordance with the Circular. Neither contractor could sufficiently document the amount of time each employee actually worked on the contracted programs. In addition, both contractors did not perform a time study.

According to the Guidance Center's CFR, Program-related payroll expenditures totaled $406,058. The Guidance Center officials reported that payroll expenditures included salaries for 25 employees. The Guidance Center officials provided us with a payroll report that was based on budget estimates calculated before the work was performed. In addition we found the time records do not show which programs the employees worked on or for how many hours, and a time study was not performed. Therefore, the Guidance Center did not have adequate records to support that the $406,058, in reported State-funded Program payroll expenditures, reflects the actual costs associated with employee work efforts.

Our findings were similar when we reviewed Palladia's documentation. According to Palladia's CFR, $7.9 million was reported as Program-related payroll expenditures for employees who worked on State-funded contract programs. We found Palladia did not have sufficient documentation to support these expenditures. Instead, Palladia provided us with documentation showing budget estimates were used to allocate employee payroll expenses among its programs.

We identified discrepancies in Palladia's payroll data and found reported payroll expenditures were not appropriate. For example, Palladia officials told us their payroll expenditures included a $284,256 salary adjustment they claimed in fiscal year 2006-07 but were reportedly for salaries paid in the 2005-06 fiscal year. However, available documentation does not support this claim and Palladia officials were unable to provide other documentation to support this charge. Palladia also could not provide allocation rates for all employees and for those that were provided we found they were not reliable.

We also reviewed a list of 87 employees who Palladia reported worked solely on one State-funded contract program and selected a judgmental sample of 35 to interview. These 35 employees had titles that were indicative of support services that would ordinarily be allocated between all Palladia programs (e.g., Director of Purchasing, receptionist, etc.). We could not speak with 21 of these employees because the employee was either not at work on the day we visited the contractor's office or the individual was no longer employed by Palladia. We interviewed the remaining 14 employees. Nine of the employees told us they worked solely on one State-funded contract program and five told us they worked on several programs including programs not funded by the State contract. For example, we interviewed two drivers and found they transported clients to and from the Palladia Admissions Office and delivered food to other programs, including those not funded by the contract. We found nine of the employees worked solely on one State-funded contract.

We conclude that neither the Guidance Center nor Palladia adhered to their State-funded contracts with respect to allocating payroll expenditures and the supporting documentation that was provided is insufficient and unreliable to support $8.3 million reported as payroll expenditures.

Administrative Expenses

Administrative expenses are costs that are not directly related to specific programs but are attributable to the overall operations of a contractor (e.g., costs for general record keeping). Administrative expenses do not include program-specific costs which should be charged directly to a program.

The Manual requires a contractor's administrative expenses be allocated to all of its State-funded programs based upon the ratio of administrative costs to total operating costs (ratio value method). Operating costs include personnel services, fringe benefits and other than personal services. Operating costs do not include equipment, property, and raw material.

Of the $11.8 million in Program-related expenditures we reviewed, $2.9 million was reported as administrative expenses by Palladia and $64,786 was reported by the Guidance Center. We found most of these expenditures were not adequately supported. We reviewed the process that both contractors used for allocating the expenditures in the CFR and found that neither of them used the ratio-value method, as required, to allocate administrative expenses.

The Guidance Center allocated Program-related administrative expenses to each program at a rate of 10 percent of direct costs. In instances where estimated total costs resulted in losses to the Program, the allocation was reduced to 8 percent. Palladia charged all of its administrative expenses directly to one State-funded contract program instead of allocating it among its eight State-funded contract programs, as required. While OASAS approved Palladia's budget which showed Palladia's intent to charge all administrative expenses to a single program, OASAS policy requires contractors to use the ratio value method or another approved method. OASAS officials confirmed that they did not approve an alternate method even though they did approve Palladia's budget. We believe OASAS officials should have rejected the budget because administrative expenses were not allocated among all State-funded programs.

Further, when we reviewed Palladia's CFR, we identified several questionable administrative charges. For example:

- We interviewed Palladia's community liaison who said his job duties included representing Palladia and its 29 programs (both State-funded and non-State-funded programs) in the community. This included holding positions on various community boards and advocacy groups, traveling to Albany to testify before the Legislature and working with elected officials. This individual's entire salary of $64,423 was reported on one State-funded contract. His salary should have been allocated based on the ratio value.
- We identified administrative payroll transfers totaling $133,179. Officials explained they transfer payroll costs to programs with available funding. Since this reallocation in not based on an employee's actual work effort, these reallocations are not allowed.
- Office and computer equipment totaling $10,515 was purchased without OASAS approval. Further, the Manual prohibits equipment purchases from being reported as an administrative cost.

We also found other expenses such as client meals, public transportation for staff and special events charged as Program-related administrative expenses. While some of these could be acceptable direct Program-related expenses, we question why they were classified as administrative expenses.

Rent and Related Expenses

The Manual requires rent and related expenses that are incurred for State-funded programs that share the same geographic location, to be allocated among all programs benefiting from those resources. The Manual further states that the preferred and most common method used to allocate these expenditures is based on actual square footage occupied by each program. We found the Guidance Center did not allocate rent or related expenses appropriately.

During the audit period, the Guidance Center reported rent and related expenses totaling $71,702 ($55,533 for rent and $16,169 for related expenses). The Guidance Center operates four Programs at one location, two of which were funded by the OASAS contract. Officials did not provide sufficient information on how they calculated the allocation rates for rent and related expenses. We reviewed the lease agreement and floor plan. We determined the rent allocation was not correct since several of the spaces were used by both State-funded and non-State funded programs yet some of the space was only charged to the State-funded program. For example, the two largest rooms were the nursery rooms, which were charged only to the OASAS contract. We found the nursery rooms were used by a non-State funded contract program as well. Since rent allocations were not accurate, the related expenses charged, which used the same allocation method, were also inaccurate.

Palladia officials stated that for the Program we reviewed they had no direct rent expenditures. However, for the period, Palladia reported other than personal service expenditures (e.g., utilities) of $2.1 million for the program reviewed. We selected six other than personal service expenditures accounts totaling $1.3 million, of which we judgmentally reviewed the largest individual transactions totaling $453,822. Two of these accounts pertained to utilities totaling $415,481. We found Palladia did not allocate the utility expenses according to the Manual. Palladia operates two programs from a single location, one of which was a State-funded contract program. Two utility companies provided services to this location. We reviewed documentation supporting the utility expenditures and found Palladia allocated 90 percent of one of the utilities and 100 percent of the other utility to the State contract. However, Palladia officials could not justify these allocations nor could they explain why different allocation methodologies were used to allocate the utilities.

Considering our audit findings, we believe OASAS should audit all Program-related expenditures for other Palladia and the Guidance Center contract years to determine whether the contractors can support their reported expenditures and to determine whether they were for contract-funded programs.

OASAS Monitoring

OASAS is responsible for inspecting and monitoring the programs it licenses and funds, to guarantee quality of care, and to ensure compliance with State and national standards, including confirming State funds are appropriately used and supported. We attribute our findings, in part, to ineffective oversight. OASAS did not audit these contracts. Instead, periodic fiscal reviews were performed. Officials told us these reviews were designed to bring providers into compliance with contractual requirements. They also stated reviews generally do not result in the recovery of unsupported expenditures unless OASAS identifies a material deficiency relating to an unapproved or inappropriate expenditure. Funds are not recovered when inappropriate or unsupported allocation methodologies are identified and contractors are not required to resubmit a corrected CFR unless OASAS has made a determination that a substantial or material deficiency has been identified. We conclude that for the providers included in our sample, these reviews did not result in providers fully complying with their contract nor did they correct all of the deficiencies OASAS previously found.

OASAS staff uses a Fiscal Review Instrument (Instrument) when conducting a fiscal review. We found it to be fairly comprehensive but the questions do not result in reviewers obtaining the information needed to determine whether contractors are properly allocating and reporting expenditures in accordance with contract requirements. For the four fiscal reviews for Palladia and the Guidance Center we examined, we found the reviewers rarely requested supporting documentation to confirm provider's statements. We found OASAS reviewers generally accepted minimal explanations for expenditures and how allocation methodologies were developed. For example, we found the two reviews at the Guidance Center, one in 2002 and the other in 2004, questioned how its rent was allocated among programs, similar to our findings. In the 2002 review, documentation showed the reviewer asked the Guidance Center officials to supply its rent allocation methodology. However, only rent allocation percentages were obtained. There was no evidence in the files that the Guidance Center supplied the actual methodology used to calculate these rates.

OASAS conducted another review in 2004, indicating the provider still could not support its allocation methodologies. However, the reviewer did not report this deficiency as a finding and no corrective action was taken. Since neither reviewer's documentation could support OASAS' efforts to determine that the Guidance Center's methodology was reasonable and accurate, we conclude that OASAS reviewers did not perform sufficient work to confirm the allocation rates are valid. Reviewers should obtain sufficient information to determine whether contractor allocation methodologies comply with requirements. We also determined that the Instrument used to conduct fiscal reviews was insufficient to determine full contract compliance for it does not require reviewers to obtain or review support documentation to verify that expenditures were Program-related, to verify that information in the CFR was accurate, or to assure appropriate allocation methodologies were used.

We further found that the Guidance Center's contract did not clearly define the services to be provided and OASAS could not provide workscope for two of the three contracted programs. Similarly, OASAS could not provide workscopes for all of Palladia's contracted programs. To monitor contracts appropriately, you must have clear service deliverables. When we reviewed OASAS' contracts and the workscope for the Guidance Center, we found these were not always specific as to what services were to be provided. Therefore, OASAS could not adequately monitor contract compliance. For example, the Guidance Center's contract does not define the services to be provided or who should receive the services for any of its three programs.

One of the programs received $128,750 for the year ending June 30, 2006 (approximately 30 percent of the total funds). However, OASAS officials could not provide documentation indicating what this program was for or what services should be provided.

We conclude that OASAS needs to strengthen its monitoring of these contracts. While OASAS conducts fiscal reviews every two or three years, this may not be sufficient to ensure contract compliance. Even when the fiscal reviews were performed, they did not result in Palladia and the Guidance Center fully adhering to the Manual and Circular, when required.

Recommendations

1. Recover the $8,032,665 in Program charges from Palladia, and the $346,223 in Program charges from the Guidance Center, they could not adequately document as Program-related.

2. Fully enforce the Manual and Circular requirements. When contractors do not comply with these requirements and all other governing statutes, recover State funds, as appropriate.

   (Recommendation number 2 revised as a result of OASAS response to draft report.)

3. Audit all Program-related expenditures for other Palladia and Guidance Center contract years to determine whether the related charges are supported and Program appropriate. Recover all unsupported and inappropriate expenditures.

4. Require reviewers to obtain sufficient information to determine whether contractors are in compliance with the Manual and the Circular, when required.

5. Revise the fiscal review instrument to include questions that would require reviewers to verify expenditure documentation and contract compliance.

6. Develop contracts and program workscopes that clearly define funded programs and services to be provided.

7. Follow-up with the Guidance Center to determine what services you are funding and assess the Program appropriateness of those services. If necessary, refer findings to the appropriate government officials.

Agency Comments

OASAS NEW YORK STATE
OFFICE OF ALCOHOLISM & SUBSTANCE ABUSE SERVICES
Improving Lives. *Addiction Services for Prevention, Treatment, Recovery*

GOVERNOR
David A. Paterson

COMMISSIONER
Karen M. Carpenter-Palumbo

December 11, 2009

Frank Patone, CPA
Audit Director
NYS Office of the State Comptroller
Division of State Government Accountability
123 William Street – 21st Floor
New York, New York 10038

Dear Mr. Patone:

I am in receipt of your draft audit report (Report 2007-S-60) *"New York State Office of Alcoholism and Substance Abuse Services: Chemical Dependency Program Payments to Selected Contractors in NYC."* The enclosed comments represent the Office of Alcoholism and Substance Abuse Services' (OASAS) response to the draft audit report and we ask that you carefully consider these prior to issuing the final audit report.

OASAS believes strongly in the importance of proper accountability in the expenditure of public funds and welcomes this opportunity for an external and objective analysis of its protocols and methods for monitoring contract compliance. At the same time, OASAS also believes it and its contractors should be held accountable based on a standard of reasonableness and ask that OSC reconsider some of the narrative and recommendations that either overstate the nature of concerns identified or call for significant recoveries above and beyond the conditions and/or costs that were questioned. We believe the most important determination should have been that services were provided, clients received treatment and community needs were addressed. * Comment 1

As these concerns have been previously communicated to the OSC Audit team both in written responses and in the Audit Exit Conference, we can only reiterate our strong desire to see the findings and recommendations of the report be more properly aligned with the nature and extent of the deficiencies identified.

We thank you for your consideration of these important points and look forward to prompt resolution of all OSC audit findings.

Sincerely,

Charles W. Monson

Charles W. Monson
Associate Commissioner
Quality Assurance and Performance Improvement

Enclosure
cc w/enc.: Karen M. Carpenter-Palumbo
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Thomas Lukacs

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*See State Comptroller's Comments, page 29.

OASAS' Response to OSC Report 2007-S-60
"New York State Office of Alcoholism and Substance Abuse Services: Chemical Dependency Program Payments to Selected Contractors in NYC"

Executive Summary

In the third paragraph of *Audit Results-Summary*, OSC states that the total amounts of unsupported Program-related expenditures exceeded the total amount the contractors were paid. Since the scope of this audit was primarily limited to the allocation of shared expense categories (utilities, lease payments, payroll, administrative expense), OASAS questions how the determination was made that all expenditures were unsupported. If the allocation methodologies used could not be documented, this would lead one to conclude that recoveries should be made for any expense exceeding a reasonable allocation of those costs, not the total amount expended. * Comment 2

In the fifth paragraph, OSC states that contractors are required to allocate administrative expenses based on the ratio of each program's operating cost to total operating expenses. While this may be the preferred method, other methods are permissible in the DMH claiming schedules, providing the alternative methods are reasonable and appropriately documented. * Comment 3

Introduction

In the fourth paragraph, OSC suggests that under the "net deficit" approach, OASAS automatically applies a "dollar-for-dollar" reduction in funding for any revenue generated which exceeds the originally budgeted amount. While OASAS may choose to reduce State funding when revenues exceed the budgeted amount, this is a discretionary determination which is made in the context of other factors, including the potential reinvestment of excess revenues to expand or enhance program operations in other areas. * Comment 4

In the sixth paragraph, OSC indicates that the Consolidated Fiscal Report (CFR) requires State-funded contract programs to keep records of actual time worked for employees assigned to funded programs. In fact, the CFR requires contract agencies to document the time and effort of shared staff between different programs using an acceptable basis of allocation or time studies, not actual time worked. * Comment 5

Audit Findings and Recommendations

On page 13, second paragraph – please refer to the comments above under Executive Summary.

Payroll Expenses

On page 15, the OSC wording in the first paragraph relative to net deficit funding and supportable expenditures is confusing and unclear. OASAS recommends deleting this sentence since it confuses two unrelated issues – net deficit funding (a funding mechanism) versus supporting documentation (an accountability expectation). * Comment 5

Also, on page 15, in its closing statement on Payroll Expenses, OSC reports that they could not verify that the $8.3 million reported as Program-related expenditures were used for Program-related purposes. However, in the narrative that precedes this statement, OSC reported that they interviewed 14 employees, * Comment 5

*See State Comptroller's Comments, page 29.

all of whom worked either full time or part time on the state-funded program. While it may be true that neither program could document a satisfactory basis for allocating shared staff time, the fact remains that OSC verified that staff were paid to perform program-related work. Rather than stating they could not verify $8.3 million was used for program-related purposes, OSC should more accurately state that an acceptable basis of allocating shared staff time could not be documented.

*Comment 5

Administrative Expenses

In the second paragraph on page 15, OSC states that contractors are required to allocate administrative expenses based on the ratio of each program's operating cost to total operating expenses. To be correct, the ratio value method is required to allocate agency administrative expense between State agencies. However, within OASAS programs (on the DMH schedules), another allocation may be used. As previously communicated to OSC, OASAS agrees that allocating all administrative costs in one program could create a situation where administrative expenses are not fully conveyed for each program. Subsequent to the 2005-06 contract period, OASAS did require Palladia to allocate its administrative expenses across all of its programs.

*Comment 5

OASAS Monitoring

On pages 17 through 19, OSC questions the value of OASAS' fiscal reviews, the primary fiscal monitoring approach with regard to fiscal and contractual requirements. A fiscal review is limited in scope and focuses on overall fiscal management policies and systems as a way to assure compliance with State requirements. When deficiencies are identified, OASAS uses a "corrective action plan" approach with contractors as opposed to audit disallowances (which are more typically associated with in-depth audits such as those conducted by OSC). The fiscal review approach assures broader and more frequent coverage of the OASAS service delivery system, while allowing for periodic in-depth audits when the need arises. OASAS concurs that a fiscal audit represents a more comprehensive approach to preventing misuse of State funds; however, it also requires a significantly greater investment of staff time and resources. With the current freeze on hiring and projections for significant budget deficits in the coming year, OASAS does not envision that it will be practical to adopt a more in-depth audit approach anytime in the foreseeable future.

On page 17, in the context of the discussion on unsupported allocation methodologies, OSC states that contractors are not required to submit a corrected CFR. In fact, OASAS does require submission of corrected CFRs when it has made a determination that a substantial or material deficiency has been identified. OASAS has not considered unsupported allocation methodologies to rise to this level.

*Comment 5

More importantly, on page 18, OSC states that OASAS' fiscal reviews did not result in corrected deficiencies. While this may true with regard to the unsupported allocation methodology finding at Queens Child Guidance Center, six of the total seven findings from that review were corrected.

*Comment 5

*See State Comptroller's Comments, page 29.

In the last paragraph on page 18, OSC states that contract services were not clearly defined and workscopes could not be provided for all programs. The contracts did contain an Appendix D (Program Descriptions) which set forth basic requirements and levels of care a provider is expected to adhere to for each service delivery category it provides While workscopes are not specifically incorporated into the body of OASAS' funding contracts, they are referenced in the contract and used each year as a contract performance guide. Workscopes typically identify the units of service to be delivered, number of staff delivering services, performance targets to be achieved and desired program completion rates. The location and nature of services provided are further defined by the program's Operating Certificate, which is renewed on an ongoing basis and subject to routine, on-site regulatory compliance reviews. OASAS believes that the combination of these two monitoring mechanisms is more than sufficient for purposes of assessing compliance.

* Comment 6

Regrettably, workscopes could not be provided for all programs. The example cited during the audit was the original proposal submitted by Queens Child Guidance Center for its "Asian Program." This proposal was no longer available because it had been destroyed, consistent with OASAS' records retention schedules and the uniform guidelines established by the State Education Department, OSC and the NYS Attorney General. OASAS conveyed to the OSC audit team its intent to reexamine its records retention standards as they relate to 5-year contract documentation.

* Comment 5

Finally, in the third paragraph on page 19, reference is made to undocumented immigrants and potential violations of New York State Social Services Law. OASAS communicated previously to OSC that it had confused the requirements for Medicaid and other entitlement programs (which are based on U.S. citizenship) with OASAS' net deficit funding, which is intended to cover the cost of services <u>not</u> covered by other payers. There is no prohibition – in law or in contract – relative to providing chemical dependence services to undocumented immigrants. For purposes of accuracy, OASAS strongly recommends that OSC delete narrative which suggests that undocumented immigrants are ineligible for services other than emergency medical care.

The report goes on to suggest that OASAS was unaware that State funds were being used in this manner. To the contrary, OASAS was aware that immigrants of Asian descent had received chemical dependence services. It could not, however, validate how many of the immigrants served might have been undocumented. In April and July 2009, OASAS conducted an on-site targeted review of the case records maintained for clients served in the Queens Child Guidance Center's Asian Program during the July 2005 to June 2006 period. Of a total 118 admissions during this period, 81 case records were randomly selected for review. Seven (i.e., 9%) of the 81 case records did not have sufficient documentation to prove legal residency.

<u>Recommendations:</u>

1. **Recover the $8,032,665 in Program charges from Palladia, and the $346,223 in Program charges from the Guidance Center, they could not adequately document as Program-related.**

   OASAS agrees that for any charges that cannot be adequately documented or supported as program-related, recoveries may be warranted. OASAS initiated on-site follow-up audits at Palladia and Queens Child Guidance Center in 2009. It is expected that the follow-up audits will be completed and reports issued by June 2010 which will identify specific recommended recoveries for charges that could not be supported or documented as program-related.

*See State Comptroller's Comments, page 29.

2. **Fully enforce the Manual and Circular requirements. When contractors do not comply with these requirements and all other governing statutes, such as the Social Services Law, recover State funds, as appropriate.**

OASAS believes that the role of enforcing contractual and funding requirements is an essential one. While our fiscal review process and protocols enable us to routinely conduct on-site fiscal compliance reviews of a general nature, they do not constitute a full audit, with the capacity to examine compliance with all requirements. OASAS acknowledges the importance of in-depth audits and will be looking to build its capacity to increase the number done each year. Since resources are limited, such audit activity will need to be driven by a risk-assessment process that identifies priority programs for audits.

* Comment 5

3. **Audit all Program-related expenditures for other Palladia and the Guidance Center contract years to determine whether the related charges are supported and Program appropriate. Recover all unsupported and inappropriate expenditures.**

As indicated in the response to Recommendation #1, OASAS has undertaken follow-up audits at both Palladia and Queens Child Guidance Center for the 2005-06 contract year (the period of the OSC audit). If OASAS determines that recoveries are warranted for unsupported or inappropriate expenditures, it will also examine comparable charges in the periods prior to and subsequent to 2005-06 to determine if similar recoveries are necessary.

4. **Require reviewers to obtain sufficient information to determine whether contractors are in compliance with the Manual and the Circular, when required.**

As indicated in the response to Recommendation #2, OASAS is looking to strengthen its audit capacity by expanding the number of full audits conducted. It will also augment its fiscal monitoring activities by implementing a risk-driven desk audit function and a fiscal compliance self-assessment protocol for contractors. Through these expanded activities, OASAS expects to significantly increase its capacity to monitor compliance with the above-referenced guidance documents.

5. **Revise the fiscal review instrument to include questions that would require reviewers to verify expenditure documentation and contract compliance.**

OASAS will examine potential changes that could be incorporated into its Fiscal Review Instrument that will help to identify providers that are noncompliant with CFR requirements as they pertain to the proper allocation of expenses. In the future, OASAS will also reinforce the need to validate that allocation reports or time studies are completed in instances where a shared staff arrangement is identified.

6. **Develop contracts and program workscopes that clearly define funded programs and services to be provided.**

OASAS has revised its 5 year contracts to make them more consistent with OSC's standard multi-year agreements. These contracts include a new Appendix A-1 with agency specific clauses, new Appendix C (payment and reporting schedule) detailing required actions prior to payment processing and a revised Appendix O (contract certification) requiring an annual review of a contractors performance levels.

*See State Comptroller's Comments, page 29.

7. Follow-up with the Guidance Center to determine what services you are funding and assess the Program appropriateness of those services. If necessary, refer findings to the appropriate government officials.

Since 2006, the Queens Child Guidance Center has been funded through the New York City Department of Health and Mental Hygiene (DOHMH). OASAS will continue working closely with DOHMH and Queens Child Guidance Center to develop service performance targets which will be regularly monitored by both agencies during the course of the funding year. OASAS has scheduled an interim on-site review of Queens Child Guidance Center in January 2010 to evaluate program performance, during which the program appropriateness of services will be assessed. DOHMH will be invited to participate in this review.

State Comptroller's Comments

1. Our stated audit objective was to determine whether payments were appropriate and adequately supported based on compliance requirements. We did not determine or assess delivery of program services.
2. It is accurate to say that our findings generally pertained to the absence of documentation supporting an acceptable allocation methodology for expenses as well as some specific instances of inappropriate costs being allocated to State programs. These findings are the basis for our conclusions that Program-related costs were unsupported in amounts that exceed the total amount the contractors were paid for deficit funding. Consequently, we recommended recovery of State contract payments. However, we also recognize that lack of support for expenses does not mean that no program services were provided. Consequently, we have revised our report to clarify that OASAS officials should determine specific recoveries to be made based on the results of their program assessments and follow-up auditing.
3. We agree with OASAS officials that more than one method may be used for cost allocations provided the methods are reasonable and appropriate. Our report was revised to reflect this point. However, as our report also indicates, the methodology in use by the contractors was not documented or understandable.
4. Our report does not state that OASAS automatically applies a "dollar-for-dollar" reduction in funding for any revenue generated which exceeds the originally budgeted amount. In addition, it should be noted that any expansion of contract programs, funding or otherwise, would be subject to formal multi-agency review processes and cannot be implemented unilaterally by OASAS.
5. We have revised our report to reflect the comments of OASAS officials.
6. Except for one contracted program, OASAS officials did not provide us with documentation to support work scope.